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**Federal Deposit Insurance Corporation**

550 17th Street, NW, Washington, DC 20429-9990

Legal Division

December 13, 2016

In re: FDIC FOIA Log Number 16-0289

This is in response to your May 24, 2016 Freedom of Information Act (FOIA) request for a copy of the following four FDIC Office of Inspector General publications:

EVAL-16-001

AUD-14-006

EVAL-12-003

Audit Report 06-016

Our records search has been completed, and all of the records that you requested have been located.

We are granting your request in part. I have enclosed copies of the records that are being disclosed, which consist of 123 pages.

The information withheld is exempt from disclosure under FOIA Exemptions 4, 5, 6 and 7(E), 5 U.S.C. § 552(b)(4), (b)(5), (b)(6) and (b)(7)(E). Exemption 4 requires us to withhold trade secrets, and confidential or privileged commercial or financial information that was submitted by a person. Exemption 5 allows us to withhold inter-agency or intra-agency memorandums or letters which would not be available by law to a party other than an agency in litigation with the agency (i.e., information that is privileged to the FDIC). Exemption 6 requires us to withhold personnel and medical files and similar files the disclosure of which would constitute a clearly unwarranted invasion of personal privacy. Exemption 7(E) requires the withholding of records or information compiled for law enforcement purposes to the extent that the production of such law enforcement records or information would disclose techniques and procedures for law enforcement investigations or prosecutions, or would disclose guidelines for law enforcement investigations or prosecutions if such disclosure could reasonably be expected to risk circumvention of the law.

You may contact me at 703-562-2274 or [aliturner@fdic.gov](mailto:aliturner@fdic.gov) or our FOIA Public Liaison, Acting FDIC Ombudsman Gordon Talbot, by email at [GTalbot@fdic.gov](mailto: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](mailto: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.

Sincerely,

/Signed/

Alisa Turner  
Government Information Specialist  
FOIA/Privacy Act Group



# Office of Inspector General

August 2006  
Report No. 06-016

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**Controls Over the Disposal of Sensitive  
FDIC Information by Iron Mountain, Inc.**

## AUDIT REPORT

This Report Contains Confidential  
Information  
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*Office of Audits*





## Background and Purpose of Audit

In carrying out its mission, the FDIC creates and acquires a significant amount of sensitive information. Much of this information is required to be protected by federal statutes and regulations. It is, therefore, critical that the FDIC implement appropriate controls when disposing of sensitive information to prevent an unauthorized disclosure that could lead to potential legal liability or public embarrassment.

The FDIC's Division of Administration (DOA) has overall responsibility for the FDIC's records management program, including the disposition of official hardcopy and electronic records no longer needed to conduct business. In 2000, DOA awarded a contract to Iron Mountain, Inc.<sup>®</sup> (Iron Mountain) for nationwide records management services, including the disposal of sensitive FDIC records. The FDIC's headquarters offices disposed of approximately 168,000 pounds of sensitive and non-sensitive records from July 2005 through February 2006, primarily due to consolidation of headquarters office space.

The objective of the audit was to determine whether the FDIC has adequate controls for ensuring the secure disposal of sensitive information by Iron Mountain. The audit focused on the disposal of information contained in shredder bins and consoles provided by Iron Mountain for the FDIC's headquarters offices.

## Controls Over the Disposal of Sensitive FDIC Information by Iron Mountain, Inc.

### Results of Audit

The FDIC established a number of key controls to ensure the secure disposal of sensitive information by Iron Mountain. Such controls include a corporate policy on records disposal; policies and procedures related to contractor integrity, fitness, and background investigations; and contractual requirements governing the destruction of information. In addition, no instances of unauthorized disclosure or use of sensitive FDIC information came to our attention during the audit. However, as reflected in the table below, the FDIC needed to improve its oversight of the Iron Mountain contract to ensure that controls designed to safeguard the disposal of sensitive information were effectively implemented. We also identified certain other matters relating to subcontractor costs and agreements and the identification of FDIC's records management contractors that warrant management attention.

Controls for Safeguarding the Disposal of Sensitive Information	Establishment of Control	Implementation of Control
Independent Audits and Trade Certifications	Needs Improvement	Needs Improvement
Integrity, Fitness, and Custody of Sensitive Information	√ *	Needs Improvement
Background Investigations	√	Needs Improvement
Authorization of Contractor Personnel	√	Needs Improvement
Supervision of Records and Media Destruction	√	Needs Improvement
Certificates of Destruction	√	Needs Improvement
On-site Inspections of Disposal Operations	√	Needs Improvement

\* Indicates that the control is in place.

### Recommendations and Management Response

We recommended that the Director, DOA:

- Consider the results of independent operational audits and recognized trade association certifications before approving disposal firms.
- Require all firms providing records disposal services on behalf of the FDIC to comply with FDIC acquisition policies and procedures.
- Establish clear expectations regarding contractor and subcontractor oversight for contracted records management services.
- Perform periodic site inspections of firms providing records disposal services.
- Ensure that subcontractor invoices and agreements are consistent with FDIC policy and the Iron Mountain contract.
- Identify all firms providing records management services for the FDIC.

DOA management's comments and planned actions were responsive to the recommendations.

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**Federal Deposit Insurance Corporation**  
3501 Fairfax Drive, Arlington, VA 22226

Office of Audits  
Office of Inspector General

**DATE:** August 10, 2006

**MEMORANDUM TO:** Arleas Upton Kea  
Director, Division of Administration

(b)(6)

**FROM:**   
Russell A. Rau  
Assistant Inspector General for Audits

**SUBJECT:** *Controls Over the Disposal of Sensitive FDIC Information  
by Iron Mountain, Inc.*  
(Report No. 06-016)

This report presents the results of our audit of the FDIC's controls over the disposal of sensitive hardcopy records and electronic media<sup>1</sup> by the Corporation's records management contractor, Iron Mountain, Inc.<sup>®</sup> (Iron Mountain).<sup>2</sup> The audit focused on the disposal of information contained in shredder bins and consoles provided by Iron Mountain for the FDIC's headquarters offices. The objective of the audit was to determine whether the FDIC has adequate controls for ensuring the secure disposal of sensitive information by Iron Mountain. Appendix I of this report discusses our audit objective, scope, and methodology in detail. Appendix II contains a glossary of terms.

## BACKGROUND

In fulfilling its legislative mandate of insuring deposits, supervising financial institutions, and managing receiverships, the FDIC creates and acquires a significant amount of sensitive information, such as financial institution examination ratings, pending enforcement actions, and personally identifiable information of depositors. The FDIC also creates a wide range of sensitive information related to its employees, such as personnel files, health records, attorney-client privileged information, and Equal Employment Opportunity complaint files. Much of the information managed by the FDIC falls within the scope of several statutes and regulations intended to protect such information from unauthorized disclosure. These statutes and regulations include the Privacy Act of 1974; the Federal Information Security Management Act of 2002 (FISMA); and Parts 309, *Disclosure of Information*, and 310, *Privacy Act Regulations*, of the FDIC's Rules and Regulations, which address disclosure of information and implement the Privacy Act, respectively. It is, therefore, critical that the FDIC implement appropriate controls when disposing of sensitive information to prevent an

<sup>1</sup> For the purpose of this report, the term "record" refers to both official corporate records and non-record documents (such as copies of official records). Electronic media include compact disks (CDs), floppy diskettes, microfiche, and microfilm cartridges.

<sup>2</sup> Iron Mountain is a registered trademark of Iron Mountain, Inc.

unauthorized disclosure that could lead to potential legal liability or public embarrassment for the Corporation.

To implement the records disposal requirements of the Fair and Accurate Credit Transactions Act of 2003 (FACT Act), the U.S. Federal Trade Commission (FTC)<sup>3</sup> issued a regulation entitled, *Disposal of Consumer Report Information and Records* (the Disposal Rule). The Disposal Rule, which became effective June 1, 2005, implements the FACT Act requirement that “any person that maintains or otherwise possesses consumer information, or any compilation of consumer information, derived from consumer reports for a business purpose[,] properly dispose of any such information or compilation.” The Disposal Rule requires organizations and individuals to employ “reasonable measures” when disposing of sensitive information derived from consumer reports to protect against unauthorized access to or use of the information. The FDIC’s Legal Division advised us that the FTC and the other regulators, when drafting the Disposal Rule, did not contemplate that the rule would apply to federal agencies. However, for the purposes of our audit, we considered the Disposal Rule to embody prudent business practices that the FDIC should voluntarily adopt to safeguard the disposal of its sensitive information derived from consumer reports.

The FDIC's Division of Administration (DOA) has overall responsibility for the Corporation's records management program, including the disposition of official hardcopy and electronic records that are no longer needed to conduct business. The FDIC's Chief Information Officer (CIO), who is also the Corporation's Chief Privacy Officer, is responsible for ensuring that the FDIC takes appropriate steps to protect personally identifiable information from unauthorized use, access, or disclosure. In addition, FDIC Circulars 1210.18, *FDIC Records Management Program*; 1210.1, *FDIC Records Retention and Disposal Schedule*; and 1210.4, *Records Disposition*, define corporate policy and procedures for managing and disposing of sensitive records created or acquired in the course of conducting business. Circular 1610.2, *Security Policy and Procedures for FDIC Contractors and Subcontractors*, defines criteria for assigning risk-level designations to contractor personnel to ensure their background investigations are commensurate with the criticality of their responsibilities. Further, the *FDIC Acquisition Policy Manual* (APM) contains the Corporation's policies and procedures for procuring goods and services and identifying roles and responsibilities for all FDIC employees involved in the pre-solicitation, solicitation, proposal evaluation, award, and contract administration phases of the procurement process.

On July 19, 2000, DOA awarded a contract to Iron Mountain for nationwide records management services, including the disposal of sensitive FDIC records no longer needed to conduct business. DOA expanded the scope of the Iron Mountain contract effective on February 26, 2005, to supply the FDIC's headquarters and selected regional offices with

<sup>3</sup> The FACT Act directs the FTC, the bank regulators, and others to promulgate rules regarding the proper disposal of consumer report information. In this context, the term consumer report includes information obtained from a consumer reporting company that is used, or expected to be used, to establish a consumer's eligibility for credit, employment, or insurance, among other purposes. The FTC's rule covers most businesses that use consumer report information.



shredder bins and media consoles to dispose of sensitive hardcopy records and electronic media, respectively.<sup>4</sup> [REDACTED]

[REDACTED] Iron Mountain

[REDACTED] During the period July 2005 through February 2006, [REDACTED] approximately 168,000 pounds of sensitive and non-sensitive FDIC records that had been placed in the bins by headquarters employees and contractor personnel.<sup>5</sup>

Iron Mountain [REDACTED]

[REDACTED] The Iron Mountain contract was scheduled to expire on July 31, 2006.<sup>6</sup> FDIC contracting officials advised us that they are in the process of negotiating a new contract with Iron Mountain.

## RESULTS OF AUDIT

The FDIC established a number of key controls to ensure the secure disposal of sensitive information by Iron Mountain. Such controls include a corporate policy on records disposal; policies and procedures related to contractor integrity, fitness, and background investigations; and contractual requirements governing the destruction of information. In addition, no instances of unauthorized disclosure or use of sensitive FDIC information came to our attention during our on-site visits to Iron Mountain. [REDACTED] However, the FDIC needed to improve its oversight of the Iron Mountain contract to ensure that controls designed to safeguard the disposal of sensitive information were effectively implemented. We also identified certain other matters relating to subcontractor costs and agreements and the identification of the FDIC's records management contractors that warrant management attention.

## OVERSIGHT OF THE IRON MOUNTAIN CONTRACT

The FDIC has established key controls to safeguard the disposal of sensitive information by Iron Mountain; however, the implementation of these controls needed improvement. Weaknesses in the implementation of key information disposal controls were caused primarily by a lack of effective FDIC oversight of the Iron Mountain contract. The table on the following page identifies key controls for safeguarding the disposal of sensitive information and our assessments of the FDIC's actions to ensure the controls were properly established and implemented. We identified these controls based on an analysis

<sup>4</sup> Iron Mountain does not presently supply [REDACTED] in the FDIC's regional offices.

<sup>5</sup> The large volume of records shredded during this period was attributed to the consolidation of the FDIC's headquarters offices in the first quarter of 2006.

<sup>6</sup> Subsequent to our field work, DOA informed us that the current Iron Mountain contract was extended to September 30, 2006, to allow sufficient time to negotiate a new contract.

of relevant information-security-related statutes, regulations, policies, and guidelines as well as the FDIC's own policies and procedures.<sup>7</sup> A brief description of our assessment of each control follows the table.

#### Assessments of Key Information Disposal Controls

Controls for Safeguarding the Disposal of Sensitive Information	Establishment of Control	Implementation of Control
Independent Audits and Trade Certifications	Needs Improvement <sup>a</sup>	Needs Improvement
Integrity, Fitness, and Custody of Sensitive Information	√ <sup>b</sup>	Needs Improvement
Background Investigations	√	Needs Improvement
Authorization of Contractor Personnel	√	Needs Improvement
Supervision of Records and Media Destruction	√	Needs Improvement
Certificates of Destruction	√	Needs Improvement
On-site Inspections of Disposal Operations	√	Needs Improvement

<sup>a</sup> Indicates that the control is incomplete or not operating as intended.

<sup>b</sup> Indicates that the control is in place.

#### Independent Audits and Trade Certifications

The FDIC established and implemented a number of important due diligence procedures for selecting prospective records disposal firms. However, the Corporation can strengthen its due diligence procedures when selecting firms expected to handle consumer report information on behalf of the FDIC. Specifically, the FDIC should voluntarily adopt two measures contained in the Disposal Rule: (1) review and consider the results of an independent audit of the disposal firm's operations and/or compliance with the Disposal Rule and (2) require that the disposal firm be certified by a recognized trade association. Although the FDIC is not bound by the Disposal Rule, the two referenced measures represent prudent practices that the FDIC should adopt to ensure that consumer report information is properly disposed of.

<sup>7</sup> See Appendix I for the statutes, regulations, policies, procedures, and guidelines used in the audit.

## Integrity, Fitness, and Custody of Sensitive Information

The APM requires firms proposing to provide services to the Corporation to complete the *FDIC Integrity and Fitness Representations and Certifications and Contractor Representations and Certifications*. These certifications provide assurance that, among other things, individuals providing services on behalf of the FDIC satisfy the minimum standards of integrity and fitness defined in 12 Code of Federal Regulations (C.F.R.) Part 366, *Minimum Standards of Integrity and Fitness for an FDIC Contractor*. The Iron Mountain contract prohibits the award of subcontracts to third parties that have not filed such certifications. Although Iron Mountain completed the referenced certifications,

(b)(4) [REDACTED] had not. In addition, the APM requires contractors and subcontractors to complete a *Contractor Confidentiality Agreement* when their employees have access to confidential information, work on-site at the FDIC, or have access to FDIC systems. Confidentiality agreements are intended to provide the FDIC with added assurance that contractors will properly safeguard confidential information in their custody. Iron Mountain did not execute a *Contractor Confidentiality Agreement* until January 13, 2006, more than 5 years after the contract had been awarded. Further, (b)(4) [REDACTED] had not executed *Contractor Confidentiality Agreements*.

## Background Investigations

The APM and Circular 1610.2, *Security Policy and Procedures for FDIC Contractors and Subcontractors*, state that all FDIC contracts meeting certain criteria shall be assigned a risk-level designation of high, moderate, or low.<sup>8</sup> Risk-level designations are based on the criticality of a contractor's responsibilities performed regarding the potential effect misuse of information would have on the Corporation's mission. Risk-level designations are used in determining the level of background investigation needed for contractor personnel. Circular 1610.2 states that risk-level determinations must be documented in the *Contractor Risk Level Record*. FDIC contracting officials did not prepare a *Contractor Risk Level Record* for the Iron Mountain contract because they presumed the risk associated with the contract was low. However, given the sensitivity of the information handled by Iron Mountain and its subcontractors, a higher risk-level designation may be warranted.

### Authorization of Contractor Personnel

The APM states that, unless otherwise provided in the contract, the FDIC has the right to approve proposed subcontractors before a contractor can award a subcontract. The APM also states that the decision to approve new subcontractors under an existing contract must be made in writing by the Contracting Officer and that the written approval is required before the subcontractor may begin work. In addition, the Iron Mountain contract states that the contractor "shall not engage subcontractors to perform any of its

<sup>8</sup> The circular applies to all FDIC contracts awarded after August 1, 2003, including: (1) all contracts for services greater than \$100,000; (2) contracts at any amount when contractor employees have access to FDIC facilities or network/systems; or (3) any contract at the discretion of the FDIC. The circular does not apply to contractors that access FDIC facilities on an infrequent and generally unscheduled basis.

responsibilities under this contract without the prior written approval of the FDIC.” The FDIC’s Contracting Officer did not authorize [redacted] before these firms came (b)(4) into possession of and began destroying sensitive FDIC records and electronic media.

(Prior to the end of our audit fieldwork, FDIC contracting officials approved [redacted] (b)(4)

(b)(4) [redacted] as subcontractors on the Iron Mountain contract.) In addition, the APM states that prime contractors proposing the use of subcontractors should complete a detailed *Subcontracting Plan* that defines how the prime contractor will ensure oversight and control of the subcontractor’s work. Iron Mountain did not submit a *Subcontracting Plan* (b)(4) for [redacted] to the FDIC Contracting Officer.

### Supervision of Records and Media Destruction

The Iron Mountain contract states that all disposals shall be witnessed by a full-time employee of Iron Mountain who is either a supervisor or manager acceptable to the FDIC. We conducted a pre-announced visit of [redacted] on April 13, 2006 to observe the (b)(4) firm’s [redacted]. During our on-site visit, we observed an Iron

Mountain employee witnessing the destruction of the FDIC’s hardcopy records. We also (b)(4) conducted a pre-announced visit of [redacted] on (b)(4)

(b)(4) May 3, 2006. However, [redacted] was not destroying media at the time of our visit. An Iron Mountain representative informed us that Iron Mountain staff had not visited (b)(4) [redacted] prior to our visit on May 3, 2006.

### Certificates of Destruction

According to the Iron Mountain contract, “... a signed Certificate of Destruction shall be provided to FDIC for each collection destroyed. This certificate will indicate where and when the destruction occurred ....” Although the Certificates of Destruction that we sampled for the FDIC’s hardcopy records could be tracked to specific shredder bins, they (b)(4) did not indicate that [redacted] (b)(4),(b)

(b)(4) [redacted] We did not assess the adequacy of Certificates of Destruction (6) related to electronic media because FDIC contracting officials advised us that no such certificates had been provided to the FDIC at the time of our audit.

### On-site Inspections of Disposal Operations

The APM requires contract Oversight Managers or Technical Monitors to perform inspections at the time and place of a contractor’s performance. In addition, the National Institute of Standards and Technology (NIST) Special Publication (SP) 800-53, *Recommended Security Controls for Federal Information Systems*, recommends that federal agencies verify media destruction actions. Inspecting information disposal operations provides assurance that sensitive hardcopy records and electronic media are destroyed in a timely manner, by trained and properly authorized personnel, and in accordance the terms of the contract. FDIC contracting officials had not performed an on-site inspection of the records destruction process prior to our audit.

(b)(4) During our on-site visit of [REDACTED] we concluded that, consistent with the terms of the  
 (b)(4) Iron Mountain contract, FDIC records [REDACTED] could not be read or  
 practicably reconstructed. As previously stated, we were unable to observe [REDACTED] (b)(4)  
 (b)(4) [REDACTED] was not destroying media at the  
 time of our visit.<sup>9</sup>

### Why Key Disposal Controls Were Not Implemented

The FDIC had not adopted certain due diligence procedures pertaining to the selection of firms handling consumer report information on behalf of the FDIC because such procedures are not required. In addition, FDIC contracting officials informed us that they  
 (b)(4) were aware of Iron Mountain's [REDACTED] but had  
 (b)(4) overlooked steps to ensure [REDACTED]  
 Contracting officials may have had a greater awareness of the need to subject [REDACTED] (b)(4)  
 (b)(4) [REDACTED] if the Certificates of Destruction had identified  
 where the FDIC's records were being destroyed and who was performing the destruction. Further, FDIC contracting officials indicated that they were unaware that Iron Mountain  
 (b)(4) [REDACTED] prior to our audit. (b)(4) (b)  
 (b)(4) Consequently, contracting officials had not taken action to ensure [REDACTED] (b)(4)  
 (b)(4) [REDACTED] FDIC contracting officials would have been alerted to  
 (b)(4) Iron Mountain's [REDACTED] had they attempted to perform an on-site inspection of  
 (b)(4) [REDACTED]

Finally, DOA established requirements in the APM for (1) a Contract Administration Plan for all contracts and task orders for services having a total estimated value of \$100,000 and (2) an Oversight Management Monitoring Plan to assist in performing oversight activities for complex contracts for services. We found neither of these documents in the contracting files. Preparation and use of these documents would have provided a greater understanding of the level of oversight necessary to ensure that Iron Mountain and its subcontractors met contract performance requirements.

### Conclusion and Recommendations

Although no instances of unauthorized disclosure or use of sensitive information came to our attention during the audit, weaknesses in contract oversight limited the FDIC's assurance that proper safeguards were being taken to securely dispose of sensitive information. A contracting official informed us that the FDIC was in the process of negotiating a follow-on contract with Iron Mountain and that Iron Mountain had been requested to notify the FDIC of any subcontractors that it plans to use under the new contract. The contracting official stated that DOA would follow appropriate procedures to ensure that Iron Mountain's proposed subcontractors provide the required integrity, fitness, and background investigation forms to the FDIC. We were also informed that

(b)(4) <sup>9</sup> Our visits to [REDACTED] did not constitute a comprehensive inspection of the firms' security  
 (b)(4) programs or records and media disposal operations. Such inspections are the responsibility of the FDIC.  
 (b)(4) Had we performed a comprehensive inspection of [REDACTED] security weaknesses may have  
 come to our attention.

DOA was working with security personnel to determine whether the current risk-level designation for the Iron Mountain contract was appropriate.

We recommend that the Director, DOA:

- (1) Require that the results of independent operational audits and recognized trade association certifications be considered before approving contractors and subcontractors to dispose of sensitive information on behalf of the FDIC.
- (2) Require Iron Mountain to ensure that all firms providing records disposal services on behalf of the FDIC under the Iron Mountain contract comply with the APM and Circular 1610.2, including provisions relating to integrity, fitness, custody of confidential information, FDIC approvals, and background investigations.
- (3) Establish in appropriate contract documentation clear expectations regarding contractor and subcontractor oversight when executing a new contract for nationwide records management services.
- (4) Perform periodic site inspections of the records disposal process, as prescribed by the APM, to ensure that sensitive hardcopy records and electronic media are destroyed in a timely manner, by trained and properly authorized personnel, and in accordance the terms of the contract.

#### **OTHER MATTERS WARRANTING MANAGEMENT ATTENTION**

We identified two contract oversight matters warranting management attention. Specifically, FDIC contracting officials needed to (1) ensure that payments to Iron Mountain are consistent with corporate policy related to subcontractor costs and (2) identify all contractors and subcontractors providing records management services on behalf of the FDIC nationwide to ensure the FDIC's interests are adequately protected.

##### **Subcontractor Costs**

To help contracting officials ensure that subcontractor costs billed to the FDIC are appropriate, the APM includes steps to verify that (1) the hours and labor categories claimed on contractor invoices are consistent with supporting time sheets and/or subcontractor invoices, (2) subcontractor labor has been properly pre-approved, and (3) subcontractor costs billed to the FDIC are consistent with the costs that the contractor actually paid or was billed by the subcontractor. The APM specifically states that prime contractors are prohibited from seeking reimbursement of markups of any kind on subcontractor invoices without the approval of the Associate Director, DOA, Acquisition Services Branch. We did not audit the amounts billed to the FDIC on Iron Mountain's invoices or review subcontractor agreements for consistency with the Iron Mountain contract. However, we noted that invoices submitted by Iron Mountain did not identify subcontractor costs or subcontractor participation in the destruction process.

Accordingly, we recommend that the Director, DOA:

- (5) Obtain and review Iron Mountain's subcontractor invoices and subcontracting agreements (if appropriate) related to work performed by [REDACTED] to [REDACTED] to determine whether the invoices and agreements are consistent with the APM and the Iron Mountain contract. (b)(4)

#### **Identification of FDIC Records Management Contractors**

At the close of the audit, FDIC contracting officials advised us that they had become aware of two other subcontractors, in addition to [REDACTED] that were providing records management services under the Iron Mountain contract. Contracting officials also informed us that they were working to identify other contractors and subcontractors that may have been engaged at the FDIC's regional, area, and field office locations to provide records management services. It is critical that the FDIC ensure that all of its records management contractors and subcontractors comply with the APM by protecting the FDIC's interests in such areas as privacy, confidentiality, integrity, and fitness. The planned renewal of the Iron Mountain contract provides the FDIC an opportunity to ensure such protections are in place at all FDIC locations. (b)(4)

Accordingly, we recommend that the Director, DOA:

- (6) Develop a complete inventory of contractors and subcontractors providing records management services on behalf of the FDIC at all headquarters, regional, area, and field office locations and take appropriate steps (where necessary) to protect the FDIC's interests, particularly in the areas of privacy, confidentiality, integrity, and fitness.

#### **CORPORATION COMMENTS AND OIG EVALUATION**

The Director, DOA, provided a written response to a draft of this report on July 26, 2006. The response is presented, in its entirety, in Appendix III of this report. The Director concurred with five of the report's six recommendations and partially concurred with the remaining recommendation. Based on DOA's response, all six recommendations are considered resolved, but they will remain open until we have determined that agreed-to corrective actions have been completed and are effective. DOA's response to each of the recommendations is summarized below, along with our evaluation of the response.

**Recommendation 1: Require that the results of independent operational audits and recognized trade association certifications be considered before approving contractors and subcontractors to dispose of sensitive information on behalf of the FDIC.**

**DOA Response:** DOA concurred with the recommendation. DOA stated that it is important to recognize that the attainment of an independent operational audit and trade certification by Iron Mountain is not a requirement of the current contract, which will

expire on September 30, 2006. However, DOA plans to consider the OIG's recommended actions as part of ongoing contract negotiations with Iron Mountain and incorporate such requirements into the new contract, as warranted. DOA also stated that the FDIC Oversight Manager would perform periodic reviews of Iron Mountain's disposal operations to achieve greater assurance that sensitive information is destroyed in a timely manner, by trained and properly authorized personnel, and consistent with the terms of the contract.

DOA indicated that Iron Mountain has not attained such trade association certifications. However, Iron Mountain is a member of two industry trade associations, [REDACTED] (b)(4)

(b)(4)

[REDACTED] DOA indicated that Iron Mountain considers its standards to be superior to those of NAID. DOA plans to require Iron Mountain to perform a comparison between its standards and those of NAID and will use the results of the comparison to determine whether requiring a trade certification for Iron Mountain would be beneficial. DOA also plans to ascertain whether Iron Mountain's subcontractors are certified by a trade association, but noted that it may be required to utilize subcontractors who are not certified in some cases. (b)(4)

Subsequent to the DOA Director's response, a DOA management official advised us that DOA was in the process of developing a records management manual that would include, among other things, guidance on the need to consider independent audits and trade certifications from future contractors that dispose of FDIC records.

**OIG Evaluation of Response:** The recommendation is resolved but will remain open until we have determined that agreed-to corrective action has been completed and is effective.

**Recommendation 2: Require Iron Mountain to ensure that all firms providing records disposal services on behalf of the FDIC under the Iron Mountain contract comply with the APM and Circular 1610.2, including provisions relating to integrity, fitness, custody of confidential information, FDIC approvals, and background investigations.**

**DOA Response:** DOA partially concurred with the recommendation. DOA stated that key Iron Mountain personnel are, and have been, compliant with the APM and Circular 1610.2 provisions. DOA also stated that "intermittent" contractor and subcontractor personnel working under the Iron Mountain contract were compliant with the background investigation requirements of Circular 1610.2. However, as part of its ongoing contract negotiations with Iron Mountain, DOA will require the completion of integrity and fitness certifications, contractor representations, and confidentiality agreements for both Iron Mountain and all of its proposed subcontractors. DOA will also request evidence of Iron Mountain's processes for reviewing the backgrounds of its own personnel and subcontractor personnel who are not considered key personnel. In addition, DOA will require Iron Mountain to develop a plan to ensure that all contractor and subcontractor



personnel are in compliance with FDIC policy relating to custody of confidential information, FDIC approvals, and background investigations, as appropriate.

**OIG Evaluation of Response:** We spoke with DOA management officials on August 8, 2006 regarding the response to this recommendation. DOA management officials recognized that the recommendation is intended to apply to all contractor and subcontractor personnel having access to sensitive information, not just personnel designated as key or intermittent personnel. DOA officials also informed us that they had elevated the risk-level designation on the Iron Mountain contract from low to moderate following our audit. The higher risk-level designation will afford the FDIC greater assurance that security oversight of the Iron Mountain contract is adequate. The recommendation is resolved but will remain open until we have determined that agreed-to corrective action has been completed and is effective.

**Recommendation 3: Establish in appropriate contract documentation clear expectations regarding contractor and subcontractor oversight when executing a new contract for nationwide records management services.**

**DOA Response:** DOA concurred with the recommendation. To ensure that oversight of the Iron Mountain contract is adequate, DOA is developing a site review plan that will require the FDIC Oversight Manager or designated representative to perform periodic inspections of Iron Mountain's performance. Such actions will be consistent with NIST SP 800-53. In addition, DOA will require a subcontracting plan that addresses contractor and subcontractor oversight expectations as part of the new Iron Mountain contract. The site review plan will include procedures to evaluate Iron Mountain's adherence to the subcontracting plan.

**OIG Evaluation of Response:** Subsequent to the DOA Director's response, a DOA management official advised us that, in addition to considering guidelines in NIST SP 800-53, DOA would consider all relevant NIST guidelines, including draft SP 800-88, *Guidelines for Media Sanitization*, to ensure appropriate measures are taken to dispose of sensitive FDIC information. The recommendation is resolved but will remain open until we have determined that agreed-to corrective action has been completed and is effective.

**Recommendation 4: Perform periodic site inspections of the records disposal process, as prescribed by the APM, to ensure that sensitive hardcopy records and electronic media are destroyed in a timely manner, by trained and properly authorized personnel, and in accordance the terms of the contract.**

**DOA Response:** DOA concurred with the recommendation. In its response, DOA stated that the FDIC Oversight Manager would conduct periodic site inspections of the records disposal process under the new Iron Mountain contract. In addition, the FDIC Oversight Manager will evaluate Iron Mountain's compliance with the subcontracting plan discussed in response to Recommendation 3.

**OIG Evaluation of Response:** The recommendation is resolved but will remain open until we have determined that agreed-to corrective action has been completed and is effective.

**Recommendation 5: Obtain and review Iron Mountain's subcontractor invoices and subcontracting agreements (if appropriate) related to work performed by** (b)(4)   **to determine whether the invoices and agreements are consistent with the APM and the Iron Mountain contract.**

**DOA Response:** DOA concurred with the recommendation. DOA indicated that the disposal services reviewed under the audit were billed to the FDIC at fixed-unit prices that were determined to be fair and reasonable. As part of DOA's ongoing contract negotiations, Iron Mountain's rates for disposal services will be evaluated for reasonableness. DOA stated that invoices for the Iron Mountain contract have been reviewed and are consistent with the terms of the contract and FDIC policy.

**OIG Evaluation of Response:** On August 8, 2006, we spoke with DOA management officials regarding the response to this recommendation. DOA management officials stated that the restrictions on subcontractor mark-ups described in the APM are not intended to apply to fixed-price-type contracts for which pricing is determined to be fair and reasonable. However, the management officials indicated that the APM is not clear in this regard and that appropriate clarification would be made as part of a planned project to update the APM. DOA management officials also stated that the site review plan and subcontracting plan described in response to Recommendation 3 would provide added assurance that subcontractor services are performed consistent with the terms of the contract. The recommendation is resolved but will remain open until we have determined that agreed-to corrective action has been completed and is effective.

**Recommendation 6: Develop a complete inventory of contractors and subcontractors providing records management services on behalf of the FDIC at all headquarters, regional, area, and field office locations and take appropriate steps (where necessary) to protect the FDIC's interests, particularly in the areas of privacy, confidentiality, integrity, and fitness.**

**DOA Response:** DOA concurred with the recommendation. DOA stated that it would identify and inventory all subcontractors as part of its ongoing negotiations with Iron Mountain. DOA also stated that it would take all necessary steps to protect the FDIC's interests in the areas of privacy, confidentiality, integrity, and fitness.

**OIG Evaluation of Response:** We also spoke with DOA management officials on August 8, 2006 regarding the response to this recommendation. DOA management officials stated that actions to address this recommendation would include the identification of all contractors and subcontractors providing records management services on behalf of the FDIC. The recommendation is resolved but will remain open until we have determined that agreed-to corrective action has been completed and is effective.

## APPENDIX I

## OBJECTIVE, SCOPE, AND METHODOLOGY

## Objective

The objective of the audit was to determine whether the FDIC has adequate controls for ensuring the secure disposal of sensitive information by Iron Mountain. We conducted our audit work in accordance with generally accepted government auditing standards during the period March through June 2006.

## Scope and Methodology

The scope of the audit was limited to the disposal of sensitive hardcopy records and electronic media contained in shredder bins and media consoles provided by Iron Mountain in the FDIC's headquarters offices. To accomplish the audit objective, we evaluated the adequacy of the FDIC's controls for safeguarding the disposal of sensitive information as defined in the Iron Mountain contract (as amended). Specifically, we evaluated relevant provisions of the Iron Mountain contract for consistency with the APM and FDIC Circulars 1210.4, *Records Disposition*, and 1210.11, *Official Records and Personal Papers*. We also evaluated the Iron Mountain contract for consistency with applicable federal laws, regulations, policies, and guidelines related to the disposal of sensitive information.

We interviewed the FDIC's Contracting Officer, contract Oversight Manager, and other officials who had responsibility for overseeing Iron Mountain's disposal of sensitive information. We also interviewed representatives of Iron Mountain and its

(b)(4) [REDACTED] In addition, we observed the removal of sensitive information from selected FDIC headquarters buildings and performed on-site visits of (1) Iron Mountain's storage facility in Jessup,

(b)(4) Maryland; (2) [REDACTED]  
(b)(4) [REDACTED] The audit did not include an evaluation of the FDIC's controls over the destruction of sensitive electronic media or information technology (IT) equipment performed by the Division of Information Technology (DIT).<sup>10</sup>

## Laws and Regulations

In conducting our audit, we considered the following statutes, rules and regulations, and policy.

- **FISMA.** FISMA (codified at Title 44, United States Code (U.S.C.) Chapter 35) requires federal agencies, including the FDIC, to develop, document, and implement an agency-wide information security program that provides security

<sup>10</sup> DIT Policy, *LAN [Local Area Network] Management Media Sanitization*, permits DIT local area network management and DIT's Client Services Branch staff to sanitize or destroy sensitive electronic media or IT equipment.

## APPENDIX I

for the information and systems that support the operations and assets of the agency, including those provided or managed by another agency, contractor, or other source. FISMA directs agencies to have an annual independent evaluation performed of their information security program and practices and to report the results of the evaluation to the Office of Management and Budget (OMB).

- **The Privacy Act of 1974.** The Act (5 U.S.C. § 552a) imposes various requirements on federal agencies (including the FDIC) whenever they collect, create, maintain, and distribute records (as defined in the Act and regardless of whether they are in hardcopy or electronic format) that can be retrieved by the name of an individual or other identifier. The Act also requires appropriate technical, administrative, and physical safeguards to ensure the security and confidentiality of records and protection from hazards to their security.
- **Freedom of Information Act.** The Act (5 U.S.C. § 552) contains disclosure requirements for federal records (including those of the FDIC), including requests for information by the general public. Certain types of records are exempt from the disclosure requirements, including privileged records, law enforcement records, and records that would affect personal privacy or confidential commercial information.
- **FACT Act.** This Act amends the Fair Credit Reporting Act (15 U.S.C. Chapter 41) by adding provisions regarding the accuracy of information in consumer reports, protection in the case of identity theft, the proper disposal of credit report information, etc. Some provisions of the Fair Credit Reporting Act apply to the FDIC.
- **Title 44, U.S.C. Chapter 33.** The provisions of this chapter govern the disposal of federal records. The FDIC follows those provisions as a matter of policy as expressed in FDIC Circular 1210.18, *FDIC Records Management Program*.
- **Federal Deposit Insurance Act (FDI Act), sections 12(f)(3) and (4).** See Appendix II of this report (*Minimum Standards of Integrity and Fitness*) for further information.
- **FDIC Rules and Regulations.** Part 309, *Disclosure of Information*, sets forth the basic policies of the FDIC regarding information it maintains and the procedures for obtaining access to such information. Part 310, *Privacy Act Regulations*, establishes regulations implementing the Privacy Act of 1974 by delineating the procedures that an individual must follow in exercising access or amendment rights under the Privacy Act to records maintained by the FDIC in systems of record. Part 366, *Minimum Standards of Integrity and Fitness for an FDIC Contractor*, establishes the minimum standards of integrity and fitness that contractors, subcontractors, and employees of contractors and subcontractors must meet if they perform any service or function on behalf of the FDIC. (FDIC's regulations are codified at Title 12, C.F.R.)
- **OMB Circular No. A-130, Management of Federal Information Resources, Appendix III, Security of Federal Automated Information Resources (OMB A-130 Appendix III).** OMB A-130 Appendix III requires agencies to establish controls to assure adequate security for all information processed, transmitted, or stored in federal automated information systems. OMB A-130 Appendix III defines adequate security as security commensurate with the risk

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and magnitude of harm resulting from the loss, misuse, or unauthorized access to or modification of information.

- **Disposal Rule.** The Disposal Rule requires organizations and individuals to employ “reasonable measures” when disposing of sensitive information derived from consumer reports to prevent the unauthorized access to or use of information. The FDIC’s Legal Division advised us that the FTC and the other regulators, when drafting the Disposal Rule, did not contemplate that the rule would apply to federal agencies. However, for the purposes of our audit, we considered the Disposal Rule to embody prudent business practices that the FDIC should voluntarily adopt to safeguard the disposal of its sensitive information derived from consumer reports.

In addition, we evaluated the FDIC’s controls for disposing of sensitive information under the Iron Mountain contract for consistency with relevant provisions of NIST SPs 800-53, *Recommended Security Controls for Federal Information and Information Systems*, and 800-53A, *Guide for Assessing the Security Controls in Federal Information Systems*. Although these documents are not legally binding on the FDIC, they contain government-wide security recommendations that agencies are expected to follow.

### Prior Audit Coverage

The OIG performed a prior audit of Iron Mountain’s records management and storage operations to determine whether (1) the contract for records storage was cost-effective and (2) the FDIC’s procedures were consistent with other best practices in the federal government and private industry.<sup>11</sup> In addition, the OIG conducted audit work related to the FDIC’s Privacy Program.<sup>12</sup> However, these audits did not address controls over the disposal of sensitive FDIC information by Iron Mountain.

### Internal Controls Reviewed

We identified and evaluated selected FDIC internal controls designed to safeguard the removal, transportation, temporary storage, and destruction of sensitive hardcopy records and electronic media by Iron Mountain and its subcontractors. Such controls included relevant policies, procedures, contractual provisions, and practices.

### Performance Measures, Fraud, and Illegal Acts

We did not develop specific audit procedures to assess performance measures or detect fraud and illegal acts because they were not considered material to the audit objective. However, throughout the audit, we were sensitive to the potential for fraud, waste, abuse, and mismanagement.

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<sup>11</sup> OIG Report No. 04-045 entitled, *Records Management and Storage*, dated September 30, 2004.

<sup>12</sup> OIG Reports entitled, *Response to Privacy Program Information Request in OMB’s Fiscal Year 2005 Reporting Instructions for FISMA and Agency Privacy Management*, dated September 2005 (Report No. 05-033); and *FDIC Safeguards Over Personal Employee Information*, dated January 2006 (Report No. 06-005).

## APPENDIX II

## GLOSSARY OF TERMS

Term	Definition
<b>Background Investigation</b>	<p>A generic term that describes a check or checks that DOA's Security Management Section completes on contractors and its personnel to ensure they meet minimum security, integrity, and fitness standards as set forth by the FDIC. These checks range from a fingerprint criminal records check by the Federal Bureau of Investigation to checks of various on-line databases such as Lexis/Nexis,<sup>®</sup> Dun and Bradstreet, and the General Services Administration's <i>Debarred and Suspended Bidders List</i>.</p> <p>The term also includes various types of background investigations conducted by the U.S. Office of Personnel Management for the FDIC.</p>
<b>Contractor</b>	An individual, corporation, partnership, joint-venture, or other third-party entity that enters into a contract with the FDIC to provide goods, services, or other requirements pursuant to its terms and conditions.
<b>Consumer Report</b>	The Fair Credit Reporting Act defines the term "consumer report" to include information obtained from a consumer reporting company that is used, or expected to be used, in establishing a consumer's eligibility for credit, employment, or insurance, among other purposes. Credit reports and credit scores are consumer reports, as are reports that businesses or individuals receive with information relating to employment background, check-writing history, insurance claims, residential or tenant history, or medical history.
<b>Contracting Officer</b>	The FDIC representative with delegated authority to enter into and legally bind, administer, and terminate contractual instruments on behalf of the FDIC.
<b>Disposal or Disposition of Records</b>	All actions taken when records are no longer needed to conduct business.
<b>Disposal Rule</b>	The Disposal Rule, which the FTC issued effective June 1, 2005, requires organizations and individuals to employ "reasonable measures" when disposing of sensitive information derived from consumer reports to prevent its unauthorized access or use. This regulation implements section 216 of the FACT Act, which was designed to close a loophole in prior legislation by expanding the scope of coverage of the Act.

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Term	Definition
<b>Electronic Media</b>	Includes any means for transmitting messages electronically in a format that allows visual text to be displayed on equipment, such as a personal computer monitor. Examples include CDs, floppy diskettes, microfiche, and microfilm cartridges.
<b>Local Area Network</b>	A data communications system that connects IT devices in a building or group of buildings within a few square miles, including (but not limited to) workstations, front-end processors, controllers, switches, and gateways.
<b>Minimum Standards of Integrity and Fitness</b>	The minimum standards of integrity and fitness required of individuals who provide service to or on behalf of the FDIC include regulations governing conflicts of interest, ethical responsibility, and use of confidential information in accordance with section 12(f)(3) of the FDI Act, 12 U.S.C. § 1822(f)(3), and the prohibitions and the requirements for submission of information in accordance with section 12(f)(4) of the FDI Act, 12 U.S.C. § 1822(f)(4). Part 366 of the FDIC Rules and Regulations implements these statutory provisions.
<b>Physical Security Controls</b>	Measures that prevent or deter attackers from accessing a facility, resource, or information stored on physical media. A control can be as simple as a locked door or as elaborate as multiple layers of armed guardposts.
<b>Risk</b>	The probability that a particular threat will exploit a particular vulnerability of a system.
<b>Risk-Level Designation</b>	<p>An evaluative classification designation assigned to contractor personnel based on the criticality of the responsibilities performed regarding the potential effect misuse of information would have on the Corporation's mission. Positions are classified as follows:</p> <ul style="list-style-type: none"> <li>(1) High Risk: Access to highly sensitive/critical systems or information with the potential for causing exceptionally serious damage.</li> <li>(2) Moderate Risk: Access to moderately sensitive/critical systems or information with the potential for causing moderate damage.</li> <li>(3) Low Risk: Access to systems or information with the potential for causing minimal damage.</li> </ul>

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Term	Definition
<b>Sensitive Information</b>	Sensitive data means (1) any information, the loss, misuse, modification of, or unauthorized access to, could affect the national interest or the conduct of federal programs, or the privacy to which individuals are entitled under the Privacy Act of 1974, but has not been specifically authorized under criteria established by an Executive Order or an act of Congress to be kept classified in the interest of national defense or foreign policy; and (2) sensitive records as defined in FDIC Circular 1210.4 that are generally not releasable under the Freedom of Information Act or whose access is controlled by the Privacy Act. In some instances, such records are accessible to only selected individuals within the FDIC. Examples of FDIC-generated sensitive records include personnel records, employee health records, Equal Employment Opportunity complaint files, employee ethics files, attorney-client privileged documents, and investigative case files. Examples of failed institution sensitive records include employee personnel files and asset/credit files.
<b>Subcontractor</b>	An individual, corporation, partnership, joint-venture, or other third-party entity that has entered into a contract with an FDIC contractor to perform work on behalf of the FDIC.



## APPENDIX III

## CORPORATION COMMENTS



Federal Deposit Insurance Corporation  
3501 Fairfax Drive, Arlington, VA 22226-3500

Division of Administration

July 26, 2006

**MEMORANDUM TO:** Stephen M. Beard  
Deputy Assistant Inspector General for Audits

**FROM:** Arleas Upton Kea [redacted]  
Director, Division of Administration

**SUBJECT:** Management Response to the Draft OIG Audit Report Entitled,  
*Controls Over the Disposal of Sensitive FDIC Information by Iron Mountain, Inc.*

This is in response to the subject Draft Office of Inspector General (OIG) Report, issued June 29, 2006. In its report, the OIG identified six recommendations.

We appreciate that the OIG noted that it did not find any instance of unauthorized disclosure or use of sensitive information but recognize that some weaknesses exist that warrant our attention. This response outlines our planned corrective actions for each of the recommendations cited in the OIG's Report.

#### MANAGEMENT DECISION

##### Finding: Weaknesses in Contract Oversight

**Condition:** Although no instances of unauthorized disclosure or use of sensitive information came to our attention during the audit, weaknesses in contract oversight limited the FDIC's assurance that proper safeguards were being taken to securely dispose of sensitive information.

**Recommendation 1:** That the Director, Division of Administration (DOA) require that the results of independent operational audits and recognized trade association certifications be considered before approving contractors and subcontractors to dispose of sensitive information on behalf of the FDIC.

**Management Response 1:** DOA concurs with this recommendation.

**Corrective Action:** Although DOA agrees with the OIG recommendation, it is important to note that the attainment of an independent operational audit and trade certifications by Iron Mountain (IM) was not a requirement of the current Contract. The current IM contract was scheduled to expire on July 31, 2006, but was extended to September 30, 2006, to allow sufficient time to negotiate a new contract; therefore, DOA/ASB will not seek to modify the current contract to include the recommended actions suggested by the OIG. Instead, DOA/ASB will consider the OIG's recommended actions in the negotiations that are in process with IM and will look to incorporate them and any trade certifications as deemed warranted into the new contract, expected to be awarded by September 30, 2006. DOA recognizes the need for

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audits/reviews that will review the processes and procedures of contractors and subcontractors in the disposition of sensitive information. These periodic reviews, which will be conducted by the FDIC Oversight Manager, will support compliance with the audit recommendation through the use of NIST Special Publication (SP) 800-53, *Recommended Security Controls for Federal Information Systems*, that federal agencies verify media destruction actions, as guidance. Moreover, the auditing and review of the information disposal operations will provide FDIC with the assurance that sensitive hardcopy records and electronic media are destroyed in a timely manner by trained and properly authorized personnel and in accordance the terms of the contract.

In regard to contractors and subcontractors being certified by a recognized trade association, IM has not attained such certifications, but they are members of two well-known industry trade associations. [REDACTED]

[REDACTED] IM is a leader in the industry and considers that their standards are superior to those of NAID. IM is currently in the process of becoming a member of the International Standards Organization (ISO). IM plans to adopt ISO's international standards of the industry to maintain their superior position in the marketplace. Given IM's plans, FDIC will require IM to produce a comparison between their standards and the NAID standards. FDIC will then determine if any significant benefit exists for a certification requirement. With regard to the subcontractors, we will inquire if they are certified by a trade association. However, we may be required to utilize subcontractors who may not be certified in some cases.

**Date of completion:** September 30, 2006.

**Recommendation 2:** That the Director, DOA require Iron Mountain to ensure that all firms providing records disposal services on behalf of the FDIC under the Iron Mountain Contract comply with the APM and Circular 1610.2, including provisions relating to integrity, fitness, custody of confidential information, FDIC approvals, and background investigations.

**Management Response 2:** DOA partially concurs with this recommendation.

**Corrective Action:** DOA is currently and has been in compliance with the APM and Circular 1610.2 for all key personnel working under the Contract. The FDIC is also in compliance with the background investigation requirement for contractor and subcontractor intermittent personnel as stated in Section 5, paragraph 3 of the Circular which states, "This policy shall not apply to intermittent contractors who access FDIC facilities on an infrequent and generally unscheduled basis."

As part of negotiations of the new contract, FDIC will require IM to complete Integrity and Fitness Certifications and Contractor Representations and execute Confidentiality Agreements for both IM and all proposed subcontractors. With regard to background investigations, IM will be asked to provide evidence of their corporate process for reviewing the backgrounds for both their own personnel and those of their subcontractors that are not considered key personnel. In addition, a provision will be added to the new contract requiring IM to develop a plan to ensure that all contractor and subcontractor personnel are in compliance with provisions relating to

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access and custody of confidential information, FDIC approvals, and background investigations as appropriate, relating to contractors and subcontractors as defined under Circular 1610.2.

**Date of completion:** September 30, 2006.

**Recommendation 3:** That the Director, DOA establish in appropriate contract documentation clear expectations regarding contractor and subcontractor oversight when executing a new contract for nationwide records management services.

**Management Response 3:** DOA concurs with this recommendation.

**Corrective Action:** An FDIC Site Review Plan will be included in negotiations of the new contract and a provision will be included in the new IM contract to address contractor and subcontractor oversight expectations. At this time, the Program Office is in the process of drafting a Site Review Plan that will require the FDIC Oversight Manager or their representatives to perform periodic inspections of IM's performance. This plan will include field office locations and random site visits to improve FDIC oversight of the IM Contract to ensure that controls designed in the Site Review Plan provide adequate safeguards for the disposal of sensitive information. As stated in the APM, "a prime contractor proposing the use of subcontractors should complete a detailed subcontracting plan defining how the prime contractor will ensure oversight and control of the subcontractor's work." Given this requirement, a subcontracting plan requirement will be incorporated in the new IM contract and the Site Review Plan will also consider procedures to evaluate IM's adherence to its subcontractor oversight plan. The proposed actions will use NIST Special Publication (SP) 800-53, *Recommended Security Controls for Federal Information Systems*, as guidance in verifying media destruction actions. Inspecting information disposal operations will provide assurance that sensitive hardcopy records and electronic media are destroyed in a timely manner by trained and properly authorized personnel and in accordance the terms of the contract.

**Date of completion:** September 30, 2006.

**Recommendation 4:** That the Director, DOA perform periodic site inspections of the records disposal process, as prescribed by the APM, to ensure that sensitive hardcopy records and electronic media are destroyed in a timely manner by trained and properly authorized personnel and in accordance the terms of the Contract.

**Management Response 4:** DOA concurs with this recommendation.

**Corrective Action:** FDIC's current standard procedure includes site visits by the FDIC Oversight Manager (OM), utilizing a Site Visit Checklist which is used by the FDIC (OM) or their representative on each site visit. After each site visit the OM or their representative prepares documents and provides any recommended changes or improvements if necessary to IM. The OM under the new IM contract will conduct periodic site inspections of the records and disposal process. As part of the inspection plan, the OM will be required to evaluate IM's

## APPENDIX III

compliance with its subcontracting oversight plan. As stated in our response to Recommendation 3 above, a subcontracting plan requirement will be discussed in negotiations and the result included in the new contract with IM.

**Date of completion:** September 30, 2006.

**Finding: Subcontractor Costs**

**Condition:** The APM specifically states that prime contractors are prohibited from seeking reimbursement of markups of any kind on subcontractor invoices without the approval of the Associate Director, DOA, Acquisition Services Branch. We did not audit the amounts billed to the FDIC on Iron Mountain's invoices. However, we noted that invoices submitted by Iron Mountain did not identify subcontractor costs.

**Recommendation 5:** That the Director, DOA obtain and review Iron Mountain's subcontractor invoices and subcontracting agreements (if appropriate) related to work performed by Hanna and Gemark to determine whether the invoices and agreements are consistent with the APM and the Iron Mountain Contract.

**Management Response 5:** DOA concurs with this recommendation to review the invoices. This is a firm-fixed-price Contract where services are already known and they have reasonably definable functional or detailed specifications with agreed-upon fixed unit prices for each of the operational activities defined under the Contract. IM's agreed-upon fixed unit prices were determined to be fair and reasonable for the services provided prior to award for the existing contract and will be evaluated for reasonableness as part of the negotiations of the new contract. Invoices for the current Contract have been reviewed and are in accordance with the terms and conditions of the Contract and current policy.

**Corrective Action:** None

**Finding: Identification of FDIC Records Management Contractors**

**Condition:** It is critical that the FDIC ensure that all of its records management contractors and subcontractors comply with the APM by protecting the FDIC's interests in such areas as privacy, confidentiality, integrity, and fitness. The planned renewal of the Iron Mountain Contract in July 2006 provides the FDIC an opportunity to ensure such protections are in place at all FDIC locations.

**Recommendation 6:** That the Director, DOA develop a complete inventory of contractors and subcontractors providing records management services on behalf of the FDIC at all headquarters, regional, area, and field office locations and take appropriate steps (where necessary) to protect the FDIC's interests, particularly in the areas of privacy, confidentiality, integrity, and fitness.

**Management Response 6:** DOA concurs with this recommendation.

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**Corrective Action:** All subcontractors will be identified and inventoried during negotiations of the new contract with IM and all appropriate documents and procedures will be executed before the award of the new contract. This audit recommendation will be discussed as part of negotiations and the necessary requirements will be put in place to ensure that the FDIC's interest in the area of privacy, confidentiality, integrity and fitness are protected and included in the new IM contract.

**Date of completion:** September 30, 2006.

If you have any questions regarding this response, FDIC's point of contact for this matter is Andrew Nickle. Mr. Nickle can be reached at (703) 562-2126.

cc: Ann Bridges Stealy  
Michael Rubino

## MANAGEMENT RESPONSE TO RECOMMENDATIONS

This table presents the management response on the recommendations in our report and the status of the recommendations as of the date of report issuance.

Rec. Number	Corrective Action: Taken or Planned/Status	Expected Completion Date	Monetary Benefits	Resolved: <sup>a</sup> Yes or No	Open or Closed <sup>b</sup>
1	DOA will consider independent operational audits and trade certifications as part of its ongoing contract negotiations with Iron Mountain and incorporate such requirements into a new contract, as warranted. Also, DOA will evaluate the results of a comparison between Iron Mountain's disposal standards and NAID standards. In addition, DOA will include guidance on the need to consider operational audits and trade certifications in its records management manual currently under development.	September 30, 2006	N/A	Yes	Open
2	DOA will require integrity and fitness certifications, contractor representations and certifications, and confidentiality agreements for Iron Mountain and its proposed subcontractors. Also, DOA will review Iron Mountain's background investigation processes for its personnel and proposed subcontractor personnel. In addition, DOA will require Iron Mountain to develop a plan to ensure compliance with FDIC policy regarding custody of confidential information, FDIC approvals, and background investigations. Subsequent to our field work, DOA elevated the risk-level	September 30, 2006	N/A	Yes	Open

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	designation of the Iron Mountain contract from low to moderate which will provide greater assurance that security oversight of the contract is adequate.				
3	DOA will develop a site review plan and subcontracting plan that address contract oversight expectations for the Iron Mountain contract.	September 30, 2006	N/A	Yes	Open
4	The FDIC Oversight Manager will conduct periodic site inspections of Iron Mountain's disposal operations.	September 30, 2006	N/A	Yes	Open
5	DOA has determined that prior invoices submitted by Iron Mountain are consistent with the requirements of the APM. DOA management officials also stated that the site review plan and subcontracting plan described in response to Recommendation 3 would provide added assurance that subcontractor services are performed consistent with the terms of the contract.	September 30, 2006	N/A	Yes	Open
6	DOA will develop an inventory of all contractors and subcontractors providing records disposal services on behalf of the FDIC.	September 30, 2006	N/A	Yes	Open

<sup>a</sup> Resolved – (1) Management concurs with the recommendation, and the planned corrective action is consistent with the recommendation.

(2) Management does not concur with the recommendation, but planned alternative action is acceptable to the OIG.

(3) Management agrees to the OIG monetary benefits, or a different amount, or no (\$0) amount. Monetary benefits are considered resolved as long as management provides an amount.

<sup>b</sup> Once the OIG determines that the agreed-upon corrective actions have been completed and are effective, the recommendation can be closed.

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**Federal Deposit Insurance Corporation**

3501 Fairfax Drive, Arlington, VA 22226

Office of Inspector General

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**DATE:** March 23, 2012

**MEMORANDUM TO:** Board of Directors  
Audit Committee

**FROM:** Jon T. Rymer  
Inspector General

**SUBJECT:** The National Owned Real Estate Management and Marketing  
Services Contract with CB Richard Ellis, Inc.  
(Report No. EVAL-12-003)

The attached report presents the results of the Office of Inspector General's audit of the National Owned Real Estate Management and Marketing Services Receivership Basic Ordering Agreement (ORE RBOA), contract RECVR-08-G-0151, which we performed in response to an FDIC management request. Our objectives were to determine whether costs that CB Richard Ellis, Inc. (CBRE) billed the FDIC under the ORE RBOA were supported adequately, consistent with the terms and conditions of the contract, allowable, and reasonable.

We determined that a preponderance of CBRE's claims paid by the FDIC from contract inception through July 31, 2011 were adequately supported, consistent with the terms and conditions of the contract, allowable, and reasonable. We identified \$42,015 (1 percent of amounts tested) in claims that were not consistent with the contract terms. In addition, based on the statistical sampling methodology we employed, we estimated that there is a 90-percent probability that the actual amount that the FDIC paid for CBRE claims that were not consistent with the contract terms or were not adequately supported would not be less than \$398,227, and that the actual amount of costs not adequately supported would not be less than \$57,226. We made recommendations that management disallow the \$42,015 in claims we determined through testing were inconsistent with contract terms and consider disallowing the statistically-projected questioned amounts. Management's response adequately addressed our recommendations. We also included a number of observations regarding opportunities to enhance the economy, efficiency, and effectiveness of similar existing or future FDIC contracts.

**We do not intend to publicly release the report in its entirety and distribution is for official use only. We will, however, post the Executive Summary on our public Web site. We request that you safeguard the contents of the report accordingly.**

If you have any questions, please call me at (703) 562-2166 or Stephen M. Beard, Deputy Inspector General for Audits and Evaluations, at (703) 562-6352.

Attachment





**Federal Deposit Insurance Corporation**  
3501 Fairfax Drive, Arlington, VA 22226

Office of Audits and Evaluations  
Office of Inspector General

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**DATE:** March 23, 2012

**MEMORANDUM TO:** Arleas Upton Kea, Director  
Division of Administration

Bret D. Edwards, Director  
Division of Resolutions and Receiverships

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

**SUBJECT:** The National Owned Real Estate Management and Marketing  
Services Contract with CB Richard Ellis, Inc.  
(Report No. EVAL-12-003)

This report is provided in response to your request that we audit the FDIC's contract for owned real estate management and marketing services with CB Richard Ellis, Inc. (CBRE). We found that a preponderance of CBRE's claims paid by the FDIC from contract inception through July 31, 2011 were adequately supported, consistent with the terms and conditions of the contract, allowable, and reasonable. We made two recommendations for the FDIC to disallow questioned claims that we identified during our testing and a third recommendation to consider disallowing statistically-projected questioned amounts. We also included a number of observations regarding opportunities to enhance the economy, efficiency, and effectiveness of similar existing or future FDIC contracts. Our evaluation of your response to a draft of this report is incorporated into the body of the report. Your response was sufficient to resolve the recommendations. In addition, we acknowledge and summarize CBRE's response to sections of the draft report specifically involving claims reviewed and amounts questioned.

Consistent with the OIG's established approach to the Corrective Action Closure (CAC) process, the OIG plans to limit its review of CAC documentation to those recommendations that we determine to be particularly significant. Such determinations will be made when the Division of Finance, Corporate Management Control (CMC) advises us that corrective action for a recommendation has been completed. Recommendations deemed to be significant will remain open in the OIG's System for Tracking and Reporting (STAR) until we determine that corrective actions are responsive. All other recommendations will be closed in STAR upon notification by CMC that corrective action is complete but remain subject to follow-up at a later date.

**We do not intend to publicly release the report in its entirety and distribution is for official use only. We will, however, post the Executive Summary on our public Web site. We request that you safeguard the contents of the report accordingly.**

If you would like to discuss this report, please contact E. Marshall Gentry, Assistant Inspector General for Evaluations, at (703) 562-6378 or A. Michael Stevens, Evaluations Manager, at (703) 562-6381. We appreciate the courtesies extended to the audit staff.

Attachment

cc: Thomas D. Harris, Deputy Director, Acquisition Services Branch, DOA  
Gail Patelunas, Deputy Director, Receivership Operations Branch, DRR  
James H. Angel, Jr., Deputy Director, Corporate Management Control, DOF  
Daniel Bendler, Chief, Management Support Section, DOA  
Steven K. Trout, Manager, Internal Review Section, DRR  
Howard Cope, Manager, Internal Review Section, DRR  
David Chapman, Chief Statistician, Data Applications Section, DIR

# Office of Inspector General



Office of Evaluations  
Report No. EVAL-12-003

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**The National Owned Real Estate  
Management and Marketing Services  
Contract with CB Richard Ellis, Inc.**

**This report contains sensitive  
information and is for official use only.  
Other than the Executive Summary,  
the contents of the report are not  
releasable without the approval of the  
Office of Inspector General.**

March 2012



## Executive Summary

### The National Owned Real Estate Management and Marketing Services Contract with CB Richard Ellis, Inc.

Report No. EVAL-12-003  
March 2012

#### Why We Did The Audit

FDIC management requested and the FDIC Office of Inspector General (OIG) completed an audit to determine whether costs that CB Richard Ellis, Inc. (CBRE), billed the FDIC under contract RECVR-08-G-0151, the National Owned Real Estate Management and Marketing Services Receivership Basic Ordering Agreement (ORE RBOA), were supported adequately, consistent with the terms and conditions of the contract, allowable, and reasonable.

To achieve our objective, we tested a statistically valid selection of the universe of CBRE invoices under this contract that the FDIC paid from contract inception through July 31, 2011.

#### Background

The FDIC's Division of Resolutions and Receiverships (DRR) sought contractor services to assist in the acquisition, management, research and preparations for marketing, and ultimate sale of owned real estate property that the FDIC acquires as receiver of failed financial institutions. In November 2008, the FDIC executed RBOA contract RECVR-08-G-0151, effective November 14, 2008, with CBRE. The initial term of the ORE RBOA was 3 years with three options, each to extend the contract for 2 years. CBRE and the FDIC agreed in August 2011 to terminate the ORE RBOA. The FDIC's plan to transition ORE assets to other RBOA contractors was completed at the end of December 2011.

Among other things, the ORE RBOA required the contractor to

- at all times act in good faith and in the best interests of the FDIC, and use its best efforts and exercise all due care and sound business judgment in performing its duties under the RBOA;
- maintain books, records, documents, and other evidence sufficient to reflect properly all costs claimed to have been incurred in performing the contract; and
- make available records relating to the work terminated for 3 years after any resulting final settlement.

We determined that the FDIC paid CBRE \$108,319,278 (not including funding advances, which we excluded from our testing) for contract services and pass-through asset-level expense reimbursements from contract inception through July 31, 2011. The invoices comprising that amount represent our sample universe.

#### Audit Results

Based on a review of a statistically valid sample of invoice line items, we determined that a preponderance of CBRE's claims paid by the FDIC from contract inception through July 31, 2011 were adequately supported, consistent with the terms and conditions of the contract, allowable, and reasonable. Of \$4,094,787 tested from 1,623 sampled claims, we found \$42,015 (1.03 percent of amounts tested) in 129 claims (7.95 percent of the number of claims tested) that were not consistent with the contract terms in the four types of invoices that we reviewed. We found the following among the four types of claims that we tested:

**Executive Summary****The National Owned Real Estate  
Management and Marketing Services Contract  
with CB Richard Ellis, Inc.**Report No. EVAL-12-003  
March 2012

- **Asset Management Fees** – We tested 587 claims totaling \$538,464. We found that CBRE claimed and the FDIC paid \$6,969 (1.29 percent) in asset management fees that were not consistent with the contract terms.
- **Pass-Through Expenses** – We tested claims for 718 assets that comprised 2,283 individual bills (which is actually an indeterminately greater number because the detailed data that CBRE provides to the FDIC rolls up certain expenses that are contained on multiple bills). Claims tested totaled \$1,345,397. We found that CBRE claimed and the FDIC paid \$7,140 (0.53 percent) more than appropriate per the contract, which includes both incorrect and unsupported claims.
- **Labor and Travel Expenses** – We tested 163 claims totaling \$1,965,317. We found that CBRE claimed and the FDIC paid a net of \$30,996 (1.58 percent) that was not consistent with the contract terms, which includes both incorrect and unsupported claims.
- **Other Expenses** – We tested 69 other expense invoices (those not falling into one of the three areas above) in their entirety comprising \$245,609 in total claims. We found that, netting overcharges with undercharges, CBRE could have but did not claim \$3,090 (1.26 percent) more than the FDIC paid for other expenses.

Based on our testing a statistically valid sample of items that CBRE claimed and the FDIC paid in that period, we calculated an unbiased projection of questioned costs to be \$742,558 (0.69 percent of the sample universe). In addition, we estimated that there is a 90-percent probability that the actual amount of CBRE claims that should be questioned would not be less than \$398,227, and that the actual amount of costs not adequately supported would not be less than \$57,226. These projections reflect certain instances in which CBRE could have but did not make allowable claims.

We made three recommendations for the FDIC to disallow components of the questioned claims. We plan to report \$398,227 as total questioned costs, and report \$57,226 as unsupported costs in the OIG's next Semiannual Report to the Congress. The amount ultimately disallowed by the FDIC could change based on final management decisions after evaluating the findings and recommendations included in the report.

In addition, we are including a number of observations, while neither within the scope nor fully evaluated as part of this audit, regarding opportunities to enhance the economy, efficiency and effectiveness of similar existing or future FDIC contracts.

**Management Comments**

The Directors of the Division of Administration and the Division of Resolutions and Receiverships jointly provided a written response, dated March 6, 2012, to a draft of this report. In the response, the Directors concurred with the two recommendations to disallow questioned costs that were not consistent with the contract terms, net of claims that CBRE could have but did not make, and that CBRE could not adequately support as consistent with the contract terms. Regarding the third recommendation, the Directors acknowledged that the projected questioned costs may be statistically valid, but decided not to pursue collection of projected questioned costs based on the low error rate in the sample and the probability that collection costs would exceed recoveries.

## **Executive Summary**

# **The National Owned Real Estate Management and Marketing Services Contract with CB Richard Ellis, Inc.**

Report No. EVAL-12-003  
March 2012

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We also provided CBRE with sections of the draft report specifically involving claims reviewed and amounts questioned. In a letter to our office responding to the report, CBRE acknowledged the audit results, but requested that language in the report associated with unsupported expenses and questioned claims be clarified. Further, CBRE questioned whether statistical projections were appropriate considering the firm used prudent judgment and acted in good faith and in the best interests of the FDIC in performing its duties under the ORE RBOA. We considered CBRE's comments in finalizing our report.

Because this report includes sensitive information, we do not intend to publicly release the report in its entirety. We will, however, post this Executive Summary to our public Web site.

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**Federal Deposit Insurance Corporation**  
3501 Fairfax Drive, Arlington, VA 22226

Office of Audits and Evaluations  
Office of Inspector General

**DATE:** March 23, 2012

**MEMORANDUM TO:** Arleas Upton Kea, Director  
Division of Administration  
  
Bret D. Edwards, Director  
Division of Resolutions and Receiverships

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

**SUBJECT:** The National Owned Real Estate Management and  
Marketing Services Contract with CB Richard Ellis, Inc.  
(Report No. EVAL-12-003)

FDIC management requested and the FDIC Office of Inspector General (OIG) completed an audit to determine whether costs that CB Richard Ellis, Inc. (CBRE), billed the FDIC under contract RECVR-08-G-0151, the National Owned Real Estate Management and Marketing Services Receivership Basic Ordering Agreement (ORE RBOA), were supported adequately, consistent with the terms and conditions of the contract, allowable, and reasonable.

To achieve our objective, we tested a statistically valid selection of the universe of invoices under this contract that the FDIC paid from contract inception through July 31, 2011. Appendix 1 presents additional details on our objective, scope, and methodology. Appendix 2 describes our statistical sampling methodology.

## **BACKGROUND**

The FDIC's Division of Resolutions and Receiverships (DRR) sought contractor services to assist in the acquisition, management, research and preparations for marketing, and ultimate sale of owned real estate property that the FDIC acquires as receiver of failed financial institutions. Due to the widely varying size and types of assets from failed institutions, scalability and flexibility of the contractor's workforce was essential.

On November 13, 2008, the FDIC executed RBOA contract RECVR-08-G-0151, effective November 14, 2008, acting as receiver for various institutions and in its corporate capacity with CBRE, a Delaware corporation with a principal place of business in Washington, D.C. The ORE RBOA provided for services to assist the FDIC in the



identification, acquisition, managing, and marketing (sales and disposition) activities of all ORE assets.

Among other things, the ORE RBOA required the contractor to

- at all times act in good faith and in the best interests of the FDIC, and use its best efforts and exercise all due care and sound business judgment in performing its duties under the RBOA;
- maintain books, records, documents, and other evidence sufficient to reflect properly all costs claimed to have been incurred in performing the contract; and
- make available records relating to the work terminated for 3 years after any resulting final settlement.

We determined that the FDIC paid CBRE \$108,319,278 from contract inception through July 31, 2011, not including funding advances<sup>1</sup> to bank accounts that CBRE would use to pay expenses allowed under the contract. We excluded invoices for funding advances from our testing because the actual expenses claimed from the advances would be tested by our sample of remaining invoices and amounts that the FDIC paid. Our audit applied a statistical sampling methodology with reasonable target precision to allow us to project our results across the universe of invoices that the FDIC paid CBRE under the contract through July 31, 2011. Those invoices represent our universe as shown in Table 1.

**Table 1: Contract Invoices Paid by the FDIC through July 31, 2011**

Invoice Type	Number	Value	Tested	Sampled Value
Asset Management Fees	1,376	\$25,874,899	61	\$538,464
Pass-Through Expenses	1,410	\$75,625,827	63	\$1,345,397
Labor and Travel Expenses	172	\$5,312,234	73	\$1,965,317
Other Expenses *	269	\$1,506,318	69	\$245,609
Invoices Eligible for Testing	3,227	\$108,319,278	266	\$4,094,787

Source: OIG analysis of a DRR data extract from the FDIC's New Financial Environment.

\* Other expenses invoices are those that were not one of the three other invoice types.

The initial term of the ORE RBOA was 3 years with three options, each to extend the contract for 2 years. (b)(4),(b)(5)

(b)(4),(b)(5)

(b)(4),(b)(5)

The FDIC and CBRE (b)(4),(b)(5)

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

and agreed to terminate the ORE

RBOA. The FDIC's plan to transition ORE assets to other RBOA contractors was completed at the end of December 2011.

<sup>1</sup> The audit also excluded \$1,010,984 paid for pass-through expenses based on incorrectly classifying the invoice as a funding advance.

## AUDIT RESULTS

We determined that a preponderance of CBRE's claims paid by the FDIC from contract inception through July 31, 2011 were adequately supported, consistent with the terms and conditions of the contract, allowable, and reasonable. Of \$4,094,787 tested from 1,623 sampled claims, we found \$42,015 (1.03 percent of amounts tested), including \$19,462 in costs the audit determined to be inadequately supported, in 129 claims (7.95 percent of the number of claims tested) that were not consistent with the contract terms in the four types of invoices that we reviewed.<sup>2</sup> Based on testing a statistically valid sample of items that CBRE claimed on invoices that the FDIC paid from contract inception through July 31, 2011,<sup>3</sup> we calculated an unbiased projection of the questioned costs for the audit universe (claims that CBRE made and the FDIC paid from contract inception through July 31, 2011) to be \$742,558. In addition, we estimated that there is a 90-percent probability that the actual amount that the FDIC paid for CBRE claims that were not consistent with the contract terms or were not adequately supported would not be less than \$398,227.<sup>4</sup> The projection incorporates our findings that, in some cases, CBRE could have but did not make some claims.

Table 2 summarizes our testing and results, which are explained more fully in subsequent sections of this report.

**Table 2: Claims Tested and Amounts Questioned**

Invoice Type	Number of Claims Tested	Amount of Exceptions to ORE RBOA Criteria	Amounts Inadequately Supported	Tested Amounts Questioned	Projected Questioned Costs
Asset Management Fees	587	\$6,969	n/a	\$6,969	\$320,770
Pass-Through Expenses	718	\$2,650	\$4,490	\$7,140	\$340,748
Labor and Travel Expenses	163	\$16,024	\$14,972	\$30,996	\$93,084
Other Expenses	155	(\$3,090)	n/a	(\$3,090)	(\$12,044)
Total	1,623	\$22,553	\$19,462	\$42,015	\$742,558

Source: OIG testing and analysis, with projections from DIR.

### Asset Management Fees

We randomly selected 61 asset management fee invoices. From those, we randomly selected 587 individual claims that totaled \$538,464.

(b)(4),(b)(5)

<sup>2</sup> Our statistical sampling methodology was developed in consultation with the Division of Insurance and Research's (DIR) Data Applications Section and is described in detail in Appendix 2.

<sup>4</sup> Because the audit found no exception with any issue that the (b)(4),(b)(5)

(b)(4),(b)(5)

We found that CBRE incorrectly claimed and the FDIC paid \$6,969 (1.29 percent) of the tested asset management fee claims, net of claims CBRE could have but did not make. Based on those results, we projected the questioned costs of the universe for asset management fees to be \$320,770. Amounts questioned included:

- 11 billing errors totaling \$14,797 (2.75 percent) that CBRE corrected prior to audit; and
- 8 billing errors totaling \$2,692 (0.50 percent) related to an FDIC duplicate payment that CBRE repaid prior to the audit.

In addition, our testing found the following amounts that the FDIC paid for CBRE claims that were not consistent with the contract terms:

(b)(4)

### **Pass-Through Expenses**

We randomly selected 63 pass-through expense invoices. From those, we randomly selected 718 claims that totaled \$1,345,397.

We found that \$2,650 (0.20 percent) of the tested CBRE pass-through expense claims that FDIC paid were not consistent with the contract terms. In addition, we found that, although required by the contract, CBRE could not adequately support an additional \$4,490 (0.33 percent) of pass-through expense claims it made and that the FDIC paid. Therefore, overall, we found that the FDIC overpaid \$7,140 (0.53 percent) of tested pass-through expenses. Based on those results, we projected the questioned costs of the universe for pass-through expenses to be \$340,748.

We determined that the following claims that CBRE made and the FDIC paid were not reasonable pass-through expenses:

(b)(4)

CBRE submitted and the FDIC paid three claims of \$350, \$1,600, and \$2,540 purportedly for (b)(4) expenses that comprised the \$4,490 that CBRE could not adequately support. As noted previously, the ORE RBOA requires CBRE to maintain and make available books, records, documents, and other evidence sufficient to reflect properly all costs claimed to have been incurred in performing the contract.

### **Labor and Travel Expenses**

We randomly selected 75 labor and travel expense invoices. Two of the 75 invoices were misclassified and we tested those with other expense invoices. From the remaining 73 invoices, we randomly selected 163 individual labor and travel claims that totaled \$1,965,317.

We found that \$16,024 (0.82 percent) of the tested labor and travel expense claims that CBRE made and the FDIC paid were not consistent with the contract terms, net of claims CBRE could have but did not make. In addition, we found that, although required by the contract, CBRE could not adequately support an additional \$14,972 (0.76 percent) of labor and travel expense claims it made and that the FDIC paid. Therefore, overall, we found that the FDIC overpaid \$30,996 (1.58 percent) of tested labor and travel expenses. Based on those results, we projected the questioned costs of the universe for labor and travel expenses to be \$93,084.

Claims that were not consistent with the contract terms included (b)(4)

(b)(4)

addition, the following are the most significant exceptions that we found to ORE RBOA criteria:

(b)(4)



The following were labor and travel expense claims that CBRE could not adequately support:

(b)(4)



## Other Expenses

We randomly selected 69 other expense invoices that comprised 155 individual claims that totaled \$245,609.

We found that \$911 (0.37 percent) of tested other expense claims that CBRE made and the FDIC paid were not consistent with the contract terms. However, we also found that CBRE could have but did not claim other expenses totaling \$4,000 (1.63 percent). Therefore, overall, we found that the FDIC underpaid \$3,089 (1.26 percent) of tested other expense claims. Based on those results, we projected the questioned costs of the universe for other expenses to be a negative \$12,044.

We determined that CBRE made and the FDIC paid the following claims that were not consistent with the contract terms:

(b)(4)

Those incorrect claims were more than offset by claims that CBRE could have but did not make for the (b)(4)

(b)(4)

## RECOMMENDATIONS

We recommend that the FDIC:

1. Disallow \$22,553 for amounts that CBRE claimed and the FDIC paid that were not consistent with the contract terms, net of claims that CBRE could have but did not make;
2. Disallow \$19,462 that CBRE claimed and the FDIC paid that CBRE could not adequately support as consistent with the contract terms; and

3. Consider disallowing an additional \$356,212, which represents the statistically valid minimum of projected questioned costs of \$398,227 less \$42,015 in questioned costs identified through items tested.

Appendix 3 of this report explains the OIG's monetary benefit terms and a summary of the questioned costs identified in this audit.

## **OBSERVATIONS REGARDING OPPORTUNITIES TO ENHANCE SIMILAR CONTRACTS**

(b)(5)







(b)(4),(b)(5)

## MANAGEMENT COMMENTS AND OIG EVALUATION

On March 6, 2012, the Directors of the Division of Administration (DOA) and DRR jointly responded to a draft of this report. In their response, they concurred with the first two recommendations: (1) to disallow questioned costs that were not consistent with the contract terms, net of claims that CBRE could have but did not make; and (2) to disallow questioned costs that CBRE could not adequately support as consistent with the contract terms. Regarding the third recommendation, the Directors acknowledged that the projected questioned costs may be statistically valid and stated that management decided not to pursue collection of projected questioned costs based on the low error rate in the sample and the probability that collection costs would exceed recoveries. Appendix 4 presents FDIC management's response in its entirety.

After we issued our draft report, we determined that adjustments were needed in our estimates of the minimum actual amounts that the FDIC paid for CBRE claims that were not consistent with the contract terms, and of costs not adequately supported. We corrected those estimates in the final report. We advised the Directors of DOA and DRR of the revised estimates and they considered them in providing their written response to the report.

We consider management's response sufficient to resolve the recommendations. In addition, with regard to the observations included in the report, an FDIC official advised us that DOA and DRR are reviewing the contract and associated processes to implement any changes as appropriate.

In addition to discussing and resolving findings directly with CBRE throughout the audit, CBRE reviewed sections of the draft report specifically involving claims reviewed and amounts questioned. In a letter to our office dated February 28, 2012, CBRE endorsed the audit's core finding that a preponderance of claims paid by the FDIC from contract inception through July 31, 2011 conformed to contract terms. In addition, CBRE questioned whether statistical projections of the questioned costs were appropriate given the firm's belief that it had made prudent business judgments and acted in good faith and in the best interests of the FDIC in performing its duties under the ORE RBOA, and exercised all due care and sound business judgment in performing its duties. Further, CBRE requested that language in the report associated with unsupported expenses and questioned claims be clarified. We considered CBRE's comments in finalizing this report.

## Objective, Scope, and Methodology

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### Objective

The objective of our audit was to determine whether costs that CBRE billed the FDIC under contract RECVR 08-G-0151, the ORE RBOA, were adequately supported, consistent with the terms and conditions of the contract, allowable, and reasonable.

We conducted this audit from August 2011 to January 2012 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

### Scope and Methodology

To accomplish our objective, we:

- Reviewed relevant records and files, including the ORE RBOA contract and select modifications, prior OIG audit or evaluation work relating to the ORE RBOA, and the DRR Asset Resolution Manual.
- Met with appropriate DOA and DRR officials to discuss the audit objective, status of the contract, and the FDIC's relationship with CBRE and to consider any of the FDIC officials' specific concerns.
- Consulted with DIR staff to develop a statistical sampling methodology with reasonable target precision to allow projections across the universe of task orders, properties, invoices, and/or total amounts billed and paid under the RBOA. (See below and Appendix 2.)
- Met with CBRE officials to gain a basic understanding of CBRE billing procedures and controls.
- Determined the number of invoices and the amounts the FDIC paid under the RBOA from contract inception through July 3, 2011, and stratified the universe based on invoice number coding into four groups: asset management fees, labor and travel expenses, pass-through expenses, and other expenses (those invoices that did not fall into the other three strata).
- Randomly selected a statistically valid sample of invoices to confirm relevant data and address the audit objective.
- Reviewed FDIC Contractor Travel Reimbursement Guidelines and the United States General Services Administration nightly lodging allowance.

## **Objective, Scope, and Methodology**

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FDIC staff not employed by the OIG supported this audit. A DRR internal review specialist provided technical advice and worked as an audit team member during audit planning and testing. In addition, a DIR statistician served as a specialist to the audit to develop the statistical sampling plan detailed in Appendix 2, advise the audit team on implementing the sampling plan, and perform the analysis included in this report projecting the results of audit testing to the universe of invoices paid under the contract from contract inception through July 31, 2011. While these DRR and DIR staff members supported the audit, throughout the audit, the OIG remained responsible for all decisions regarding the scope, methodology, and reporting of audit results.

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

Consistent with the stated objective, we did not assess the FDIC's or CBRE's overall internal control or management control structure beyond what we include in this report. We obtained data from the FDIC's and CBRE's information systems; however, we did not assess the effectiveness of information system controls.

The Government Performance and Results Act of 1993 (the Results Act) directs Executive Branch agencies to develop a customer-focused strategic plan, align agency programs and activities with concrete missions and goals, and prepare and report on annual performance plans. Such an assessment was not part of this audit's objectives. Program audits of FDIC operations review the FDIC's compliance with the Results Act.

A wide range of potential risks for fraud exist with any contract. Key fraud risks related to this audit include false claims by the contractor or subcontractors whose expenses are passed through to the FDIC, or duplicate claims by or payments to CBRE. We assessed the risk of fraud and abuse related to our objective in the course of evaluating audit evidence.

## Statistical Sampling Methodology

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### Audit Universe

The universe for this audit was all invoices that CBRE submitted to the FDIC that the FDIC paid under the contract through July 31, 2011. We identified those invoices from data provided by the DRR's Business Operations Support Section, which provided a database of invoices based on queries they run routinely. There were no CBRE invoices paid in 2008. DRR provided the data in four Microsoft Excel files listing CBRE invoices paid in 2009, 2010, January-February 2011, and March-July 2011.

The audit universe provided by DRR consisted of 3,260 invoices that the FDIC paid to CBRE from contract inception through July 31, 2011. We separated the universe into four strata (or types) based on the type of invoice, which we determined from the invoice numbering system used for this contract. Our four strata were invoiced claims for:

- Asset management fees, which are the charges that CBRE was entitled to claim based on the type, value, term of management, and other factors.
- Pass-through expenses, which are costs related to managing assets that CBRE incurred and paid for through bank accounts the FDIC established and for which CBRE submitted invoices to replenish those bank accounts.
- Labor and travel expenses, which are costs for personnel and travel expenses permitted under the contract.
- Other expenses, which comprise invoices not in the other three strata and include a range of asset management-related expenses and other costs the FDIC incurred under the contract, including the advance of funds to bank accounts for pass-through expenses.

We determined that 33 of the other expense invoices were for funding advances. We excluded those from our universe because the actual expenses claimed from those advances would be tested by our sample of remaining invoices and amounts that the FDIC paid.

### Sample Design

We consulted with the DIR Data Applications Section to identify a means to sample the available data—paid invoices—statistically. As detailed below, the audit used a randomly selected two-stage stratified sample except for other expense invoices where the audit used a randomly selected single-stage sample. The sampling plan was designed so that, within “round-off error,” items within each stratum have the same probability of selection.

## Statistical Sampling Methodology

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Our purpose was to conduct variable sampling that would allow us to estimate the quantity of overpayment in dollars in the universe of payments that the FDIC made to CBRE under contract RECVR-08-G-0151, the ORE RBOA.

Two-stage sampling was accomplished by a random selection of invoices at the first stage, followed by a random selection of line items within invoices at the second stage. The two stages of selection were conducted separately within either two or three substrata defined within each of the four primary strata (except for the other expenses stratum). The labor and travel expenses and pass-through expenses strata were segmented into large- and small-dollar- invoice substrata. The asset management fees stratum was separated into three substrata, defined by large-, medium-, and small-dollar-value invoices.

We executed the sampling plan in a manner that allowed for additional testing, if desired.

### Sample Unit

For other expense invoices, we used a single-stage sample by randomly sampling invoices and testing all the line items on each selected invoice. For the other three strata, we applied two-stage sampling where the invoices were the primary sampling unit and the specific billing lines on the invoices were the secondary sampling unit.

What the specific billing lines on the invoices represented varied depending on the type of invoice. For labor and travel expense invoices, a billing line was a travel claim for an individual. For asset management fee invoices, a billing line was the fee charged for one asset (individual property or group of properties, based on the contract) in the invoice month. For pass-through expense invoices, a billing line was the total expenses claimed for an individual asset in one month.

### Sample Size

We estimated our target total sample size considering time and resources available; precision targets for estimating universe totals; DRR's Internal Review testing experience and results; limited, high-level review of some invoices; and a rough estimate of total billing lines for invoices in each stratum from a judgmental test sample of 15-18 invoices from each stratum. Based on these factors, it was decided to select a total sample of between 1,500 and 2,000 billing lines. Where our initial estimates of the average number of billing lines per invoice for a stratum varied significantly from actual results from the sample, we worked with the statistician and adjusted, before testing, the target sample size and the overall sampling rate for a stratum or substratum.

### Source of Random Numbers for Sample Selection

The audit generated random numbers from the Defense Contract Audit Agency's (DCAA) EZ Quant (Version 1.1.1) Statistical Analysis Software, which has a random

## Statistical Sampling Methodology

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number generator function. DCAA developed and tested EZ-Quant for use in its audit processes. It is freeware, and its use and copying is unrestricted.

### Characteristics Measured

The purpose of this audit's samples was to determine the extent of overpayments (or, if negative, underpayments) resulting from inadequate support or noncompliance with contract terms. Issues that (b)(4),(b)(5) were treated as complying with contract terms.

Testing was done on the four strata of expenses and varied among the strata. For example, testing for asset management fees determined whether charges were correct for the property type and value, while testing for pass-through expenses determined that there was sufficient supporting documentation for the expenses and that the expenses were reasonable and appropriate under the contract. Within each stratum, testing was conducted consistently among all audit team members by using standardized data collection instruments.

## **Explanation of Monetary Benefit Terms and Monetary Results**

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The Inspector General Act of 1978, as amended, (1) defines the terminology associated with monetary benefits identified by auditors and (2) establishes the reporting requirements for the identification and disposition of questioned costs in audit reports. In addition, the explanations provided below indicate that the process for actual recovery of questioned costs involves various stages, evaluations of factors, and decision-making processes. The following defines the key terms associated with monetary benefits and explains how they relate to each other.

- First, auditors may identify “questioned costs” based on an alleged violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the expenditure of funds. In addition, a questioned cost may be a finding in which, at the time of the audit, a cost is not supported by adequate documentation (i.e., unsupported questioned cost); or a finding that the expenditure of funds for the intended purpose is unnecessary or unreasonable. It is important to note that the OIG does not always expect to recover 100 percent of all questioned costs.
- The next step in the process of making a decision about questioned costs is a “management decision.” This is the final decision issued by management after evaluating the finding(s) and recommendation(s) included in an audit report. The management decision must specifically address the questioned costs by either disallowing or not disallowing these costs. A “disallowed cost” is a questioned cost that management, in a management decision, has sustained or agreed should not be charged to the government.
- Once management has disallowed a cost and, in effect, sustained the auditor’s questioned costs, the last step in the process takes place which culminates in the “final action.” This is the completion of all actions that management has determined are necessary to resolve the findings and recommendation included in an audit report. Typically, in the case of disallowed costs, management will evaluate factors beyond the conditions in the audit report, such as qualitative judgments of value received or the cost to litigate, and decide whether it is in the FDIC’s best interest to pursue recovery of disallowed costs.

Based on observed results from testing a statistically valid sample of items that CBRE claimed on invoices that the FDIC paid from contract inception through July 31, 2011, summarized in Table 2 in the body of this report, we calculated an unbiased projection of questioned costs to be \$742,558. In addition, we estimated that there is a 90-percent probability that the actual amount that the FDIC paid for CBRE claims that were not consistent with the contract terms or were not adequately supported would not be less than \$398,227.<sup>5</sup> This projection reflects our findings that CBRE could have but did not make some claims.

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<sup>5</sup> As noted in Appendix 1, a DIR statistician, serving as a specialist to the audit, performed the analysis projecting the testing results to the audit universe.



## **Explanation of Monetary Benefit Terms and Monetary Results**

Our presentation of statistical projections in this report was consistent, to the extent possible, with DCAA's Guidance on Variable Sampling Policy, 11-OTS-001(R), dated January 3, 2011.

## Corporation Comments



**Federal Deposit Insurance Corporation**  
3501 Fairfax Drive, Arlington, VA 22226-3500

Division of Administration

**DATE:** March 6, 2012

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

**FROM:** Arleas Upton Kea, Director  
Division of Administration

(b)(6)

Bret D. Edwards, Director  
Division of Resolutions and Receiverships

**SUBJECT:** Management Response to the Draft OIG Audit Report Entitled, *Audit of the National Owned Real Estate Management and Marketing Services Contract with CB Richard Ellis, Inc.* (Assignment No. 2011-086)

This is in response to the subject Draft Office of Inspector General (OIG) Audit Report, issued February 3, 2012. In its report, the OIG made three recommendations to the Division of Administration (DOA) and the Division of Resolutions and Receiverships (DRR).

We appreciate the review work performed by the OIG and that as noted in its report a preponderance of CB Richard Ellis (CBRE) claims were adequately supported, consistent with the terms and conditions of the contract, allowable, and reasonable. However, we recognize that certain claims did not conform to the terms of the contract. This response outlines the planned corrective actions for each of the recommendations cited in the OIG's Report.

### MANAGEMENT DECISION

#### **Finding: Claims Paid were not Consistent with Contract Terms**

**Recommendation 1:** That the FDIC disallow \$22,553 for amounts that CBRE claimed and the FDIC paid that were not consistent with the contract terms, net of claims that CBRE could have but did not make.

**Management Response 1:** DOA and DRR concur with the recommendation.

**Corrective Action:** The DOA contracting officer will issue a written demand to CBRE to recover \$22,553. A copy of the check will be provided as proof of recovery.

**Completion Date:** June 5, 2012

## Corporation Comments

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**Recommendation 2:** That the FDIC disallow \$19,462 that CBRE claimed and the FDIC paid that CBRE could not adequately support as consistent with the contract terms.

**Management Response 2:** DOA and DRR concur with the recommendation.

**Corrective Action:** The DOA contracting officer will issue a written demand to CBRE to recover \$19,462. A copy of the check will be provided as proof of recovery.

**Completion Date:** June 5, 2012

**Recommendation 3:** That the FDIC consider disallowing an additional \$356,212, which represents the statistically valid minimum of projected questioned costs of \$398,227 less \$42,015 in questioned costs identified through items tested.

**Management Response 3:** Although DOA and DRR acknowledge that the projected questioned costs may be statistically valid, management has decided not to pursue collection of projected questioned costs based on the low error rate in the sample and the probability that collection costs would exceed recoveries.

If you have any questions regarding this response, the point of contact for DOA is (b)(6) at (703) 562-2118.

## Summary of FDIC Management's Response to the Recommendations

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This table presents FDIC management's response to the recommendations in our report and the status of those recommendations as of the date of report issuance.

<b>Rec. No.</b>	<b>Corrective Action: Taken / Planned</b>	<b>Expected Completion Date</b>	<b>Monetary Benefits</b>	<b>Resolved:<sup>a</sup> Yes / No</b>	<b>Open / Closed<sup>b</sup></b>
1	The DOA contracting officer will issue a written demand to CBRE to recover \$22,553. A copy of the check will be provided as proof of recovery.	June 5, 2012	\$22,553	Yes	Open
2	The DOA contracting officer will issue a written demand to CBRE to recover \$19,462. A copy of the check will be provided as proof of recovery.	June 5, 2012	\$19,462	Yes	Open
3	Although DOA and DRR acknowledge that the projected questioned costs may be statistically valid, management has decided not to pursue collection of projected questioned costs based on the low error rate in the sample and the probability that collection costs would exceed recoveries.	N/A	\$356,212	Yes	Closed

<sup>a</sup> Resolved – (1) Management concurs with the recommendation, and the planned, ongoing, and completed corrective action is consistent with the recommendation.

(2) Management does not concur with the recommendation, but alternative action meets the intent of the recommendation.

(3) Management agrees to the OIG monetary benefits, or a different amount, or no (\$0) amount. Monetary benefits are considered resolved as long as management provides an amount.

<sup>b</sup> Recommendations will be closed when (a) Corporate Management Control notifies the OIG that corrective actions are complete or (b) for recommendations that the OIG determines to be particularly significant, when the OIG confirms that corrective actions have been completed and are responsive.

# Office of Inspector General



Office of Audits and Evaluations  
Report No. EVAL-16-001

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## **The FDIC's Efforts to Ensure Professional Liability Claims Are Cost Effective**

**This report contains sensitive  
information and is for official use only.  
Other than the Executive Summary,  
the contents of the report are not  
releasable without the approval of the  
Office of Inspector General.**

February 2016

**Executive Summary****Office of  
Inspector General****The FDIC's Efforts to Ensure Professional  
Liability Claims Are Cost Effective**Report No. EVAL-16-001  
February 2016**Why We Did The Evaluation**

After a rigorous review of the factual circumstances surrounding the failure of an insured depository institution, the FDIC may pursue professional liability claims (PLCs) against directors, officers, and other professionals whose wrongful conduct caused losses to those failed institutions. PLCs also include direct claims against insurance carriers and contract rights inherited from the institution under fidelity bonds that institutions purchase to cover losses resulting from dishonest or fraudulent acts by their employees. To collect on these claims, the FDIC often must sue the professionals for losses resulting from their breaches of duty to the failed institution. Professional liability lawsuits are only pursued if they are both meritorious and expected to be cost effective.

Our objective was to evaluate the FDIC's efforts to ensure that PLCs are cost effective. We focused our review on the design of the FDIC's policies, procedures, and other practices associated with managing costs of PLC cases. We conducted this evaluation in accordance with the Council of the Inspectors General on Integrity and Efficiency's *Quality Standards for Inspection and Evaluation*.

**Background**

The FDIC's professional liability program is intended to maximize recoveries to receiverships and hold those officials who caused losses accountable. The FDIC's Division of Resolutions and Receiverships (DRR) and Legal Division are jointly responsible for the program. DRR Investigations and the Legal Division's Professional Liability Unit (PLU) investigate 11 claim areas for each institution failure and pursue recovery of losses by filing PLCs. The FDIC Board delegated joint authority to the DRR Director and the FDIC's General Counsel to settle, dismiss, or otherwise dispose of non-asset-related suits or claims, which includes PLCs. As such, pursuing PLCs requires a coordinated effort between DRR and PLU.

**Evaluation Results**

DRR and the Legal Division have procedures and controls in place for ensuring that PLCs are cost effective including, among other things, considering costs to pursue the claim against potential recovery sources; developing a budget for outside counsel fees; capturing PLC-related costs; seeking FDIC Board authority to sue and, where appropriate, settle claims; and drafting reports and holding meetings to periodically monitor case status. Notwithstanding these efforts, we identified additional opportunities to ensure the cost effectiveness of PLCs by

- enhancing coordination between DRR and the Legal Division,
- clarifying how the FDIC determines and reassesses PLC cost effectiveness, and
- better documenting key decisions made throughout the PLC process.

**Recommendations and Corporation Comments**

We made six recommendations to strengthen program controls to help ensure that PLCs are cost effective. The FDIC has taken or proposed actions that are responsive to our recommendations.

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

Office of Audits and Evaluations  
Office of Inspector General

**DATE:** February 11, 2016

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

Charles Yi, General Counsel  
Legal Division

(b)(6)

**FROM:** E. Marshall Gentry  
Assistant Inspector General for Evaluations

**SUBJECT:** *The FDIC's Efforts to Ensure Professional Liability Claims Are Cost Effective* (Report No. EVAL-16-001)

After a rigorous review of the factual circumstances surrounding the failure of an insured depository institution, the FDIC may pursue professional liability claims (PLCs) against directors, officers, and other professionals whose wrongful conduct caused losses to those failed institutions. PLCs also include direct claims against insurance carriers and contract rights inherited from the institution under fidelity bonds that institutions purchase to cover losses resulting from dishonest or fraudulent acts by their employees. To collect on these claims, the FDIC often must sue the professionals for losses resulting from their breaches of duty to the failed institution. Professional liability lawsuits are only pursued if they are both meritorious and expected to be cost effective.

Our objective was to evaluate the FDIC's efforts to ensure that PLCs are cost effective. We focused our review on the design of the FDIC's policies, procedures, and other practices associated with managing costs of PLC cases. Specifically, we reviewed 19 claims related to a non-statistical sample of four insured depository institutions that failed between 2009 and 2011. We selected institutions that failed earlier in the recent financial crisis to ensure sufficient time had passed for PLC activity to occur. We reviewed available documentation to validate our understanding of the FDIC's methodology for determining costs associated with PLCs and whether the financial information the FDIC uses to make PLC-related decisions was comprehensive, accurate, timely and considered throughout the life cycle of the claim.

We conducted this evaluation in accordance with the Council of the Inspectors General on Integrity and Efficiency's *Quality Standards for Inspection and Evaluation*. Appendix 1 of this report includes additional details on our objective, scope, and methodology. Appendix 2

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contains a glossary<sup>1</sup> and Appendix 3 contains a list of acronyms and abbreviations. Appendix 4 contains the Corporation's comments on this report.

## Background

The FDIC's professional liability program is intended to maximize recoveries to receiverships and hold those officials who caused losses accountable. The FDIC's Division of Resolutions and Receiverships (DRR) and Legal Division are jointly responsible for the program. DRR Investigations and the Legal Division's Professional Liability Unit (PLU) investigate 11 claim areas for each institution failure and pursue recovery of losses by filing PLCs if they are both meritorious and expected to be cost effective.<sup>2</sup> The 11 PLC types are described in Table 1 below.

**Table 1: Description of PLC Types**

PLC Type	Description
Director and Officer (D&O) Liability	Claims against former directors and officers of a failed institution for conduct that caused loss to the failed institution, such as negligence, gross negligence, or breach of fiduciary duty.
Fidelity Bond	Claims against insurers for failure to pay under a financial institution bond issued to the failed institution for covered acts.
Accountants' Liability	Claims against external or internal accountants and auditors for conduct that caused loss to the failed institution, such as breach of contract, negligence, and professional malpractice.
Attorney Malpractice	Claims against attorneys and law firms for conduct that caused loss to the failed institution, such as breach of contract, negligence, and professional malpractice.
Appraiser Malpractice	Claims against individual appraisers and appraisal firms for conduct that caused loss to the failed institution, such as breach of contract, negligence, and professional malpractice.
Insurance	In states permitting such claims, direct actions against liability insurance carriers, or actions brought as assignee of a professional liability insurance policy.
Commodity Broker	Claims against brokers or brokerage firms whose conduct in connection with the purchase or sale of commodities caused loss to the failed institution, such as breach of contract, negligence, professional malpractice, and violation of law.
Issuer	Claims against insurance brokers for conduct in connection with the issuance of insurance policies that caused loss to the failed institution, such as breach of contract and negligence.
Residential Mortgage Malpractice and Fraud	Claims against mortgage brokers, title insurance companies, closing agents, and appraisers for conduct in connection with residential mortgages that caused losses to the failed institution, such as breach of contract, breach of fiduciary duty, negligence, and professional negligence.
Securities and Residential Mortgage Backed Securities	Claims against securities brokers, brokerage firms, control persons, issuers, depositors, underwriters, and sellers in connection with the purchase or sale of securities to the failed institution, such as breach of contract, negligence, gross negligence, breach of fiduciary duty, and violation of law.

<sup>1</sup> Terms that are underlined when first used in the report are defined in Appendix 2, *Glossary*.

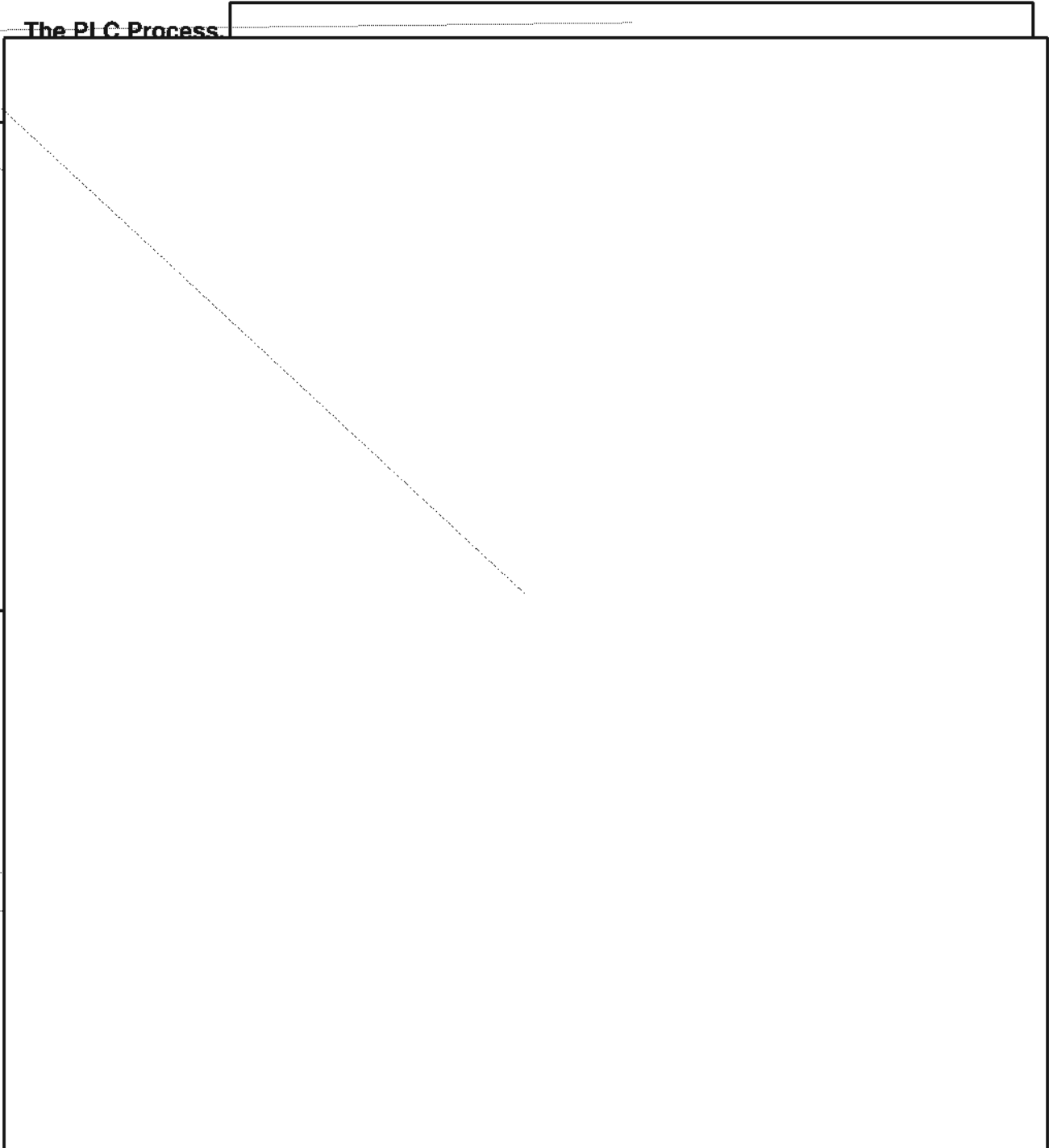
<sup>2</sup> The 1992 FDIC Board of Directors *Statement Concerning the Responsibilities of Bank Directors and Officers* explains that the FDIC only pursues PLCs that meet the two criteria. The scope of this evaluation did not include reviewing the FDIC's actions to determine a PLC's merit. We discuss how the FDIC addresses those criteria in this report only to provide context needed for the reader to understand the overall PLC process.

PLC Type	Description
Other Miscellaneous Claims	Other claims against professionals that do not fit into the other PLC types.

Source: Generated by the FDIC Office of Inspector General (OIG) based on FDIC procedures.

The FDIC Board delegated joint authority to the DRR Director and the FDIC's General Counsel to settle, dismiss, or otherwise dispose of non-asset-related suits or claims, which includes PLCs. As such, pursuing PLCs requires a coordinated effort between DRR and PLU.

#### The PLC Process



(b)(5) **Determining Merit.** [REDACTED]  
(b)(5) [REDACTED]  
(b)(5) [REDACTED] Federal and state statutes and judicial decisions establish the legal obligations of individuals and entities subject to PLCs. To show that a tort claim has merit, the FDIC generally must establish:

- Duty: the party owed a duty to the institution.
- Breach of duty: the duty was breached or violated.
- Causation: the misconduct was the cause for the loss to the institution.
- Damages: the breach of duty resulted in a loss to the institution.

(b)(5) [REDACTED] Additionally, some state laws include a business judgment rule that has been interpreted to require the FDIC to prove gross negligence to succeed on a PLC.

**Determining Cost Effectiveness.** At its simplest, for a claim to be expected to be cost effective, the FDIC's estimated recoveries should exceed its estimated costs to pursue the claim.

(b)(5) [REDACTED]

(b)(5) [REDACTED]

**Litigation Approval and Process.** When claims are deemed to be both meritorious and expected to be cost effective, the FDIC has 3 years to file tort PLCs and 6 years to file contract

(b)(5)

PLCs from the date of an institution failure, unless state law permits a longer timeframe.<sup>3</sup> If the

(b)(5)

[Redacted]

(b)(5)

[Redacted]

(b)(5)

[Redacted]

(b)(5)

(b)(5)

[Redacted]

(b)(5)

(b)(5)

[Redacted]

(b)(5)

[Redacted]

While the FDIC is fully prepared to litigate its claims against professionals of failed institutions to judgment, at any time during the process the parties may settle. Some defendants might agree to mediation either before or after the FDIC files a lawsuit, and in some cases a court may order mediation.

(b)(5)

[Redacted]

(b)(5)

[Redacted]

(b)(5)

(b)(5)

(b)(5)

**PLC Documentation.** DRR keeps PLC-related documents in various places.

(b)(5)

(b)(5)

[Redacted]

(b)(5)

(b)(5),(b)(7)

[Redacted]

(b)(5),(b)(7)

(E)

[Redacted]

(b)(5),(b)(7)

(E)

[Redacted]

<sup>3</sup> 12 U.S.C. § 1821(d)(14).

(b)(5)

[Redacted]

(b)(5),(b)(7)

(E)

[Redacted]

(b)(5),(b)(7)  
(E) [redacted]

In addition, OAs may maintain both hard-copy and electronic documents related to their cases.

**Reporting.** PLU tracks PLC recovery and expense information on an aggregate, program-wide basis and reports this information to the FDIC Board on a quarterly and annual basis. The FDIC provides an annual report to Congress, which contains information on PLC recoveries during the year, the number of authorized and filed lawsuits, the number of open investigations, and the results of annual performance goal<sup>6</sup> efforts.

Recoveries often lag expenses because of the time inherent in the litigation process that is often required to collect on PLCs. Annual recoveries can also be heavily impacted by large settlements. In a report issued in July 2014,<sup>7</sup> we recommended that the FDIC track recoveries and expenses associated with PLCs by institution, and periodically report this information to the FDIC Board and other FDIC executives. The FDIC agreed to begin reporting on recoveries and expenses by institution annually for failed institutions in which all claim areas were closed or fully resolved during the reporting period. The Legal Division issued its first such report in February 2015.

**Program Accomplishments.** From 1986 through 2014, the FDIC and former Resolution Trust Corporation<sup>8</sup> (RTC) collected \$8.62 billion from PLCs at a cost of \$2.14 billion.

From January 1, 2009, through October 23, 2015, the FDIC authorized lawsuits in connection with 150 failed institutions against 1,207 individuals for D&O liability. This includes 108 filed D&O lawsuits (70 of which have fully settled, and 1 of which resulted in a favorable jury verdict) naming 826 former directors and officers. The FDIC also has authorized 69 other lawsuits for residential mortgage-backed securities,<sup>9</sup> London Interbank Offered Rate suppression, fidelity bond, insurance, accounting malpractice, appraiser malpractice, and attorney malpractice claims. In addition, 59 residential mortgage malpractice and fraud lawsuits are pending, consisting of lawsuits filed by and inherited from failed institutions.

(b)(5) [redacted]

(b)(5)  
(b)(5) [redacted]

<sup>7</sup> Joint report of the Offices of Inspector General of the FDIC, Board of Governors of the Federal Reserve System and Consumer Financial Protection Bureau, and Department of the Treasury, *Enforcement Actions and Professional Liability Claims Against Institution-Affiliated Parties and Individuals Associated with Failed Institutions*, July 2014. The July 2014 OIG report summarized the PLC process but did not evaluate cost, recovery, and budgetary aspects. That OIG report also summarized PLC activity from 2008-2012 and factors impacting the FDIC's pursuit of PLCs.

<sup>8</sup> RTC was a temporary federal agency established in 1989 to oversee the disposal of assets from failed savings and loan institutions.

<sup>9</sup> As Receiver for failed financial depository institutions, the FDIC will file lawsuits for claims based on misrepresentations in offering documents for residential mortgage-backed securities purchased by failed institutions.

(b)(5)

## Evaluation Results

DRR and the Legal Division have procedures and controls in place for ensuring that PLCs are cost effective including, among other things, considering costs to pursue the claim against potential recovery sources; developing a budget for outside counsel fees; capturing PLC-related costs; seeking FDIC Board authority to sue and, where appropriate, settle claims; and drafting reports and holding meetings to periodically monitor case status. Notwithstanding these efforts, we identified additional opportunities to ensure the cost effectiveness of PLCs by

- enhancing coordination between DRR and the Legal Division,
- clarifying how the FDIC determines and reassesses PLC cost effectiveness, and
- better documenting key decisions made throughout the PLC process.

## Enhanced Coordination Between DRR and the Legal Division Could Help Ensure PLCs Are Cost Effective

DRR and the Legal Division jointly are responsible for carrying out the PLC program and must work together to investigate claims and pursue meritorious cases in a cost-effective manner. We identified opportunities to enhance coordination and re-evaluate DRR and PLU's respective roles in the PLC process and clarify coordination expectations within DRR and PLU guidance. Doing so could help the divisions ensure that PLCs are cost effective.

**Authorities, Roles, and Responsibilities.** Under the FDIC Bylaws, the DRR Director shall exercise general supervision and control over the performance of the Corporation's functions with respect to the activities of failing depository institutions, which includes, among other things:

- general supervision and control over the receivership and liquidation functions of the Corporation;
- establishing and liquidating claims of the Corporation as subrogee of the claims of insured depositors; and
- liquidating assets acquired by the Corporation as Receiver, liquidator, or liquidating agent of a failed institution.

The Bylaws also designate the General Counsel as the chief legal officer of the Corporation and legal adviser to the Board and the officers of the Corporation, which includes the DRR Director. The General Counsel renders all legal services necessary to enable the Board and the Corporation's various organizational units to discharge their respective duties and responsibilities, and otherwise has the powers and performs the duties usually vested in the general counsel of a corporation.<sup>10</sup>

The FDIC Board's *Delegations of Authority Relating to Receivership Management* delegate joint authority to the DRR Director and General Counsel for some receivership responsibilities.

(b)(5)

(b)(5)

Accordingly, the two divisions jointly are responsible for the professional liability program, including working together to investigate claims and ensuring those pursued are meritorious and are expected to be cost effective.

In our view, DRR and PLU need to re-evaluate their respective roles in the PLC process to reflect their delegated authorities and to help ensure that both divisions' perspectives are adequately considered in decisions involving PLCs.

(b)(5)

(b)(5),(b)

(7)(E)

#### Guidance for Coordinating PLC Activities.

(b)(5),(b)

(7)(E)

could more specifically state expectations for coordination and identify how the two divisions should work together throughout the PLC life-cycle.

<sup>10</sup> Such powers include conducting litigation, participating in any judicial or administrative proceeding, and defending the Corporation.

Identifying and Managing PLC Costs By Avoiding Duplicative Work. Both DRR and the Legal Division spend receivership funds to investigate and litigate potential claims. (b)(5)

(b)(5) [Redacted]

(b)(5) [Redacted] We were told, and case documentation suggests, that each division might not be aware of the full extent of costs incurred by the other division and the extent to which the other division retains outside contractors, OC, or experts.<sup>11</sup>

(b)(5) Opportunities may also exist to better control investigation costs and ensure that work is not duplicative. (b)(5)

(b)(5) [Redacted]

Nonetheless, given the amounts spent on investigations in relation to overall PLC expenses, DRR and the Legal Division should continue to look for opportunities to reduce investigation costs. Possible initiatives could include:

- Benchmarking cost estimates for the overall investigative work by financial institution to gauge investigation cost effectiveness.
- Increasing DRR's and the Legal Division's awareness of costs incurred and activities performed by each division for contractor and OC investigative work.
- Ensuring DRR has contractor cost controls in place if it has to rely on investigation contractors in future crises.

With the two divisions sharing the goal of identifying meritorious claims, there is a risk that OC investigative work might duplicate DRR efforts. We have been told anecdotally that this has happened, and both DRR and the Legal Division acknowledged that duplication was possible.

(b)(5) [Redacted]

(b)(5) [Redacted]

(b)(5) <sup>12</sup> [Redacted]

(b)(5) [Redacted]



To jointly implement the professional liability program efficiently and effectively, both the (b)(5) (b)(5) could better identify specific investigative roles and responsibilities between the two divisions. (b)(5)

Communicating Timely and Effectively. While DRR and the Legal Division have established procedures to support effective communication, we observed and were told that communication between DRR and the Legal Division was not always timely and effective. (b)(5)

(b)(5) (b)(5) When situations such as those occur, promptly addressing them would support efficiency that could reduce PLC costs and improve case management.

Processing Authority Memorandums. Preparing and obtaining approval for authority memorandums is an important decision point where FDIC considers the cost effectiveness of PLCs. (b)(5) (b)(5) (b)(5)

(b)(5) (b)(5) (b)(5) Based on the sample cases that we reviewed, DRR management's consideration of the proposed ATS memorandum did not occur until DRR received the ATS memorandum for signature. DRR could benefit from a documented process for vetting such memorandums.

In responding to our draft observations on this topic, regional DRR management indicated that DRR's IIC should be involved in ensuring the ATS memorandum is factually accurate along with the OA and OC, when needed. Legal Division management noted that more recently PLU will brief DRR management on the ATS memorandum, upon request.

When the FDIC pursues a PLC, the FDIC typically provides defendants an opportunity to engage in settlement discussions or mediate the claims in advance of filing a lawsuit, or a court might order mediation. (b)(5) (b)(5)

(b)(5) [redacted] In some instances, DRR management was not made aware of the proposed minimum settlement values before receiving the final memorandum for approval. More recently, DRR instituted procedures to involve its management earlier.

DRR and the Legal Division recently have instituted joint senior management briefings of cases requiring FDIC Board approval or discussion with the Chairman. Also, beginning the last quarter of 2014, DRR and the PLU began meeting regularly to review proposed ATS and authority to settle actions.

Closing PLCs. While the professional liability program has processes to monitor the timing of closing claims, it should consider a process to ensure that claims DRR and PLU agree lack merit or cost effectiveness do not incur unnecessary expense because of delays in closing them.

(b)(5) [redacted]

**Coordination Efforts Begun.** Both DRR and the Legal Division have undertaken efforts to strengthen their management of the professional liability program. DRR:

- established an Assistant Director, Investigations, position in May 2012;
- updated its [redacted] and [redacted] exhibits as part of that update;
- established a receivership operations liaison position in headquarters in late 2014 to further promote open communication and collaboration;
- now has the Assistant Director, Investigations, attend high-profile mediations, engage with counsel on a regular basis, and perform case reviews of open claims jointly with the Legal Division; and

(b)(5) [redacted] has begun updating its [redacted] from its [redacted] (b)(5)

#### DRR and the Legal Division:

- began bi-weekly phone calls in 2012 to communicate and discuss professional liability program matters as they arise;
- established more consistent management-level briefings to address questions and issues for professional liability program matters being presented to the FDIC Board and proposed settlement actions to be discussed with the FDIC Chairman; and
- in January 2015, resumed quarterly meetings, now via video teleconference, [REDACTED] (b)(5)

(b)(5)

(b)(5)

While DRR and the Legal Division have begun these efforts to better coordinate their professional liability program activities, they should jointly review and understand clearly how their respective roles and responsibilities complement each other at each stage of the PLC process, and integrate their procedures to conduct investigations, establish litigation budgets, seek authority to sue, determine minimum settlement amounts, and close cases. Jointly established protocols would help DRR and the Legal Division coordinate their work throughout the PLC process, and establish and maintain an effective partnership to implement the professional liability program efficiently and economically.

#### Recommendation

To support enhanced coordination between DRR and the Legal Division, which would help ensure PLCs are cost effective, we recommend the DRR Director and the General Counsel:

1. Review, revise, and establish guidance that:
  - more clearly defines DRR's and the Legal Division's respective roles and responsibilities to manage costs during the entire PLC life cycle;
  - delineates PLC investigation scope to aid DRR and Legal Division staff in determining the extent of their respective investigative work;
  - ensures each division's activities are communicated appropriately and coordinated throughout the PLC process, including allowing adequate opportunity to review and consider authority memorandums;
  - supports timely closing PLCs that the FDIC determines lack merit, cost effectiveness, or both; and
  - results in DRR and Legal Division expectations for coordination being consistent and complementary.

## The FDIC Should Clarify How It Determines and Reassesses PLC Cost Effectiveness

To assess an individual PLC's cost effectiveness, the FDIC considers expected recoveries in relation to estimated OC litigation costs. [REDACTED]

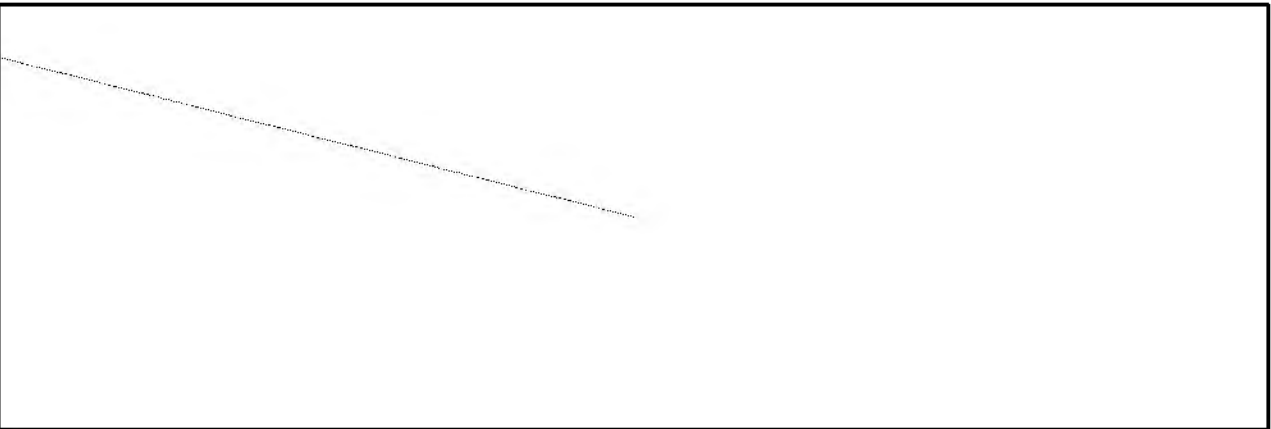
[REDACTED] Finally, because we could not readily locate documentation to support certain PLC decisions, as discussed in the following section, we could not independently determine whether the cost effectiveness of PLCs was reassessed, as required, as cases progressed. The FDIC would benefit from clarifying expectations and guidance in these areas.

**Implementing Cost-Effectiveness Criteria.** DRR's [REDACTED] refers to [REDACTED] cost-effective claims and provides steps for investigating a failed institution's 11 potential claim areas, [REDACTED] [REDACTED] The [REDACTED] does not explicitly include criteria on what costs to consider or how to determine PLC cost effectiveness.

The [REDACTED] outlines criteria for a claim to be considered cost effective. [REDACTED]

**Communicating Cost Effectiveness** [REDACTED]

(b)(5)



The FDIC also reports to the FDIC Board quarterly and annually overall professional liability program recoveries and expenses. In those reports, the FDIC includes professional liability program costs for, among other things, DRR Investigations, PLU, and other FDIC divisions' staff time; DRR contractor costs; OC fees and expert costs for investigation and litigation; and information technology (IT) and other FDIC support costs.<sup>13</sup> Beginning in early 2015, the FDIC began reporting to the Board professional liability program costs and recovery information by individual institution.

The difference in the costs considered in analyzing cost effectiveness at the claim level versus the program level creates a risk that the Board, FDIC management, and other parties involved in the PLC process might mistake what costs are considered in determining PLC cost effectiveness. We believe program understanding could be enhanced if DRR and the Legal Division clearly articulated how they determine PLC cost-effectiveness in authority memorandums.

**Allocating IT Costs to PLCs.** While some IT-related costs are captured in receivership accounts, costs the FDIC incurs related to DMS historically have not been allocated to individual programs, including PLCs, and there has been no feasible way to do so with that system. While DMS's purpose is to ensure the FDIC's compliance with legal and statutory requirements,<sup>14</sup> which is broader than just the FDIC's professional liability program, PLC investigations rely heavily on DMS information.

The portion of DMS costs that apply to the professional liability program are not included as claim or program expenses and, consequently, are not considered when the PLU determines whether a claim is expected to be cost effective or in presenting program cost effectiveness. It is presently not possible to determine what portion of DMS costs directly or indirectly support the FDIC's professional liability program. However, DMS costs that relate to the professional liability program likely are material.

<sup>13</sup> Costs reported still would not include any portion of DMS costs because the FDIC does not presently have the means to allocate such costs to the professional liability program.

<sup>14</sup> The FDIC is prohibited under 12 U.S.C. § 1821(d) (15) (D) from destroying any records of an insured depository institution for which it has been appointed receiver. The FDIC, as Receiver, must retain records going back 10 years from the date of receivership and must maintain these records for at least 6 years.

Under the FDIC's contract for DMS that became effective November 1, 2008, the FDIC paid the contractor \$427.6 million through December 31, 2014. The FDIC issued five types of DMS task orders, including ones for data capture (\$299.5 million or 70 percent of total DMS costs) and case support (\$57.5 million or 14 percent of total DMS costs). Case support is a broad category that includes a range of investigation and litigation support activity, but it is not a direct proxy for PLU support.<sup>15</sup>

The FDIC is implementing the Failed Bank Data Services (FBDS) program to replace DMS. The FDIC recognized the need to improve its functionality to provide more granular data for management to review.

(b)(5)

(b)(5)

(b)(5)

**Reassessing Cost Effectiveness.**

(b)(5)

<sup>15</sup> Case support task orders include support for commercial litigation, enforcement, requests from the OIG or criminal authorities, subpoenas from third parties, and requests from other regulators and the Division of Insurance and Research.

(b)(5)

(b)(5)

Analyzing a PLC's cost effectiveness when the FDIC receives a settlement offer will never be distilled to a specific formula and will require the PLU to apply its subjective assessment to objective financial information and facts of the case. However, it may be prudent for PLU to clarify expectations for reconsidering minimum allowable settlement amounts over time and to what extent OAs should consider, document, and discuss settlement offers with DRR.

### Recommendations

To clarify how the FDIC determines and reassesses PLC cost effectiveness, we recommend the DRR Director and the General Counsel:

2. Reassess the type of and extent to which costs related to the professional liability program are considered in determining whether a PLC is expected to be cost effective.
3. Review communications related to PLCs to ensure that program costs and costs considered in making cost effectiveness determinations are differentiated and presented clearly.
4. Clarify at which key points in the life cycle of a case the FDIC should reassess cost effectiveness.

## PLU Should Better Document Key Decisions Made Throughout the PLC Process

The Legal Division maintains electronic PLC-related documents in a SharePoint site, in   (b)(5) and on OAs' computers, as well as hard copy documents. For the PLCs that we reviewed, documentation was not always readily available to support certain financial information used in cost-effectiveness decisions, certain assumptions and cost factors, or PLC case management. Limited case documentation impacted our ability to assess the FDIC's efforts to ensure PLCs are cost effective and impacts the Corporation's ability to oversee the professional liability program. We concluded that PLU could benefit from better case documentation requirements and a central document control or case management system.

The United States Government Accountability Office (GAO) *Standards for Internal Control in the Federal Government*<sup>17</sup> explains that appropriate documentation of transactions and other significant events, which would include key decisions, should be clearly documented and readily available. In our view, good documentation is important to:

<sup>17</sup> The November 1999 edition (GAO/AIMD-00-21.3.1) is applicable to this evaluation. GAO updated the document in September 2014 (GAO-14-704G). That edition became effective beginning with fiscal year 2016.

- maintain rationale and support in the event that Corporate decisions are questioned or challenged in the future;
- set expectations for what information should be gathered and considered at various stages of the PLC process;
- facilitate management oversight and supervisory review of individual cases;
- provide a documentation trail for internal and external audit functions;
- maintain continuity in the event that staff leave the Corporation or informal forms of document storage, such as an employee's computer hard drive, fail;
- promote consistency in how case decisions are supported; and
- facilitate programmatic reviews of the program such as horizontal reviews and trend analyses.

**Support for Financial Information Used in Cost-Effectiveness Decisions.** We could not locate, through our research of PLU's SharePoint site and discussions with the OA, certain support for financial information used in cost-effectiveness decisions during the PLC process. In some cases, we could not locate documents, such as the budget for outside counsel, which provides the basis for litigation expense estimates. In other cases, documents that we did locate contained outdated, unsupported, or incorrect information, [REDACTED] (b)(5)

(b)(5)

(b)(5)

(b)(5)

(b)(5)

(b)(5)

PLU was able to provide documentation we requested in support of specific costs and estimated recovery amounts after considerable time and effort. However, it was still difficult to trace cost information within authority memorandums to supporting documents. [REDACTED] (b)(5)

(b)(5)

(b)(5)

[REDACTED] However, without a case management system or some means of documenting PLC case activity, understanding PLU's historical analyses and resulting decisions can require significant effort by PLU management to recreate, if needed, as it did for this evaluation.



**Support for Certain Assumptions and Cost Factors.** *ATS and Request for Advance Authority to Settle* memorandums provided estimated settlement amounts that were based on assumptions and cost factors for which PLU was not always able to readily explain and did not provide an audit trail. [REDACTED]

[REDACTED] Estimated settlement amounts that depend on such information could be inaccurate or not independently verifiable, and could complicate the FDIC's efforts to ensure that the related claim remains cost effective.

[REDACTED]

For another case, an OA could not readily explain during an interview how the Legal Division determined the case's estimated recovery value. Later, PLU management advised us the case had no recovery value. Better case documentation could have preserved the financial characteristics of this case to explain how the FDIC reached its recovery value conclusion.

**Case Management Documentation.** We could not locate certain budget-related documentation and the retention memorandum for a law firm hired for one of the institutions in our sample through our research of PLU's SharePoint, ALIS, or discussions with the OA. We also could not locate some or all of what we understood would be annual case reviews that PLU management holds with OAs for each of the four institutions in our sample. [REDACTED]

[REDACTED]

PLU officials ultimately located the case review documentation and clarified that case reviews were not performed exactly every 12 months or for all institutions. PLU officials noted the challenges of not having a central document control system, and mentioned that, in one case, an OA's computer hard drive failed, which resulted in a loss of supporting documentation. Those factors limit PLU's ability to manage case documentation more efficiently and effectively.

Finally, as discussed earlier, PLU could better document its reassessment of cost effectiveness as claims progress through the litigation process. Much of this consideration is done orally, according to PLU management.

Inadequate case documentation limits the FDIC's ability to ensure PLCs are cost effective and its ability to oversee the professional liability program. While PLU has strengthened its recordkeeping, including utilizing a SharePoint site for final internal documents and court documents, the unit would benefit from better case documentation requirements and a central document control or case management system that is fully searchable. Such steps would provide additional means for efficiently standardizing case files to support decisions and facilitating transitions of matters between attorneys.

Further, adequately documenting key decisions and the basis for information supporting those decisions is necessary for management and oversight review and analyses. Most federal agencies are required by the Federal Records Act (FRA) to make and preserve records containing adequate and proper documentation of the organization, functions, policies, decisions, procedures, and essential transactions of the agency. Those records should be designed to furnish the information necessary to protect the legal and financial rights of the Government and of persons directly affected by the agency's activities. The FDIC has determined that the Corporation is not covered by that Act;<sup>18</sup> however, the *FDIC Records and Information Management (RIM) Policy Manual* reflects the spirit of the Act. Specifically, the policy states that the FDIC shall maintain proper documentation of its operations, among other things, to provide current and historical data pertaining to actions taken by the FDIC, and inform decision making by FDIC officials and their successors through the use of sufficient historical data. Corporate policy also states that files should be maintained in an orderly, systematic manner so documents can be retrieved quickly and sensitive information protected.

### Recommendations

To ensure the FDIC appropriately documents the key decisions and the information used to make those decisions throughout the PLC process, we recommend the General Counsel:

5. Establish documentation expectations for PLCs and reflect such expectations in PLU procedures.
6. Consider implementing an electronic case management system for the professional liability program to include a fully-searchable repository that maintains supporting case documentation.

## Corporation Comments and OIG Evaluation

The DRR Director and General Counsel responded to a draft of this report on January 25, 2016. Following discussion with the OIG, the DRR Director and General Counsel provided a revised written response dated February 10, 2016 that clarified some of their corrective actions. That response is presented in its entirety in Appendix 4.

The DRR Director and General Counsel concurred with the report's six recommendations and described corrective actions to address each of them. The completed or planned actions are responsive and the recommendations are resolved. The response indicated that DRR and the

<sup>18</sup> FRA 44 U.S.C. Chapter 31, as amended in 1976, incorporates the agency definitions set forth in 40 U.S.C. § 102(4) and § 102(5).

(b)(5)

(b)(5)

Legal Division have completed corrective action for recommendations 2, 3, 5, and 6. Those recommendations are closed while recommendations 1 and 4 will remain open until corrective actions have been completed. Appendix 5 summarizes the Corporation's corrective actions.

## Objective, Scope, and Methodology

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### Objective

Our evaluation objective was to assess the FDIC's efforts to ensure that PLCs are cost effective. To fulfill this objective, we evaluated whether the information the FDIC uses to make decisions was comprehensive, accurate, and timely and considered throughout the life cycle of the claim.

We performed our work from April 2014 to July 2015 at the FDIC's offices in Arlington, VA and in Dallas, Texas, in accordance with the Council of the Inspectors General on Integrity and Efficiency's *Quality Standards for Inspection and Evaluation*.

### Scope and Methodology

To address our evaluation objective, we first gained an understanding of the PLC process and outlined DRR's and the Legal Division's roles in investigating and pursuing PLCs by:

- researching FDIC policy, Board delegations, and applicable laws referring to PLCs;
- reviewing DRR's Investigation Manual and the Legal Division's PLU Procedure Manual, in particular to identify how the FDIC determines cost effectiveness and how DRR and the Legal Division coordinate PLC efforts;
- determining what information and functions ALIS provides for PLCs; and
- reviewing the following audit, evaluation, and oversight reports:
  - GAO, *FDIC and RTC Could Do More to Pursue Professional Liability Claims*, GAO/T-GGD-92-42, June 1992.
  - FDIC OIG, *Audit of the Professional Liability Claims Process*, Audit Report No. 02-019, May 2002;
  - FDIC Legal Division, *PLG Visitation Report*, July 2003.
  - Offices of Inspector General of the FDIC, Board of Governors of the Federal Reserve System and Consumer Financial Protection Bureau, and Department of the Treasury, *Enforcement Actions and Professional Liability Claims Against Institution-Affiliated Parties and Individuals Associated with Failed Institutions*, Report numbers EVAL-14-002, 2014-SR-B-011 and OIG-CA-14-012, respectively, July 2014.<sup>19</sup>

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<sup>19</sup> The report summarized the PLC process but did not evaluate cost, recovery, and budgetary aspects. The report also summarized PLC activity from 2008-2012 and factors impacting the FDIC's pursuit of PLCs.

## Objective, Scope, and Methodology

We then assessed the FDIC's methodology for determining costs associated with PLCs by:

- identifying what cost and expected recovery information is used, and how timely, accurate, and complete that information is;
- determining what analysis is performed with the information used, and what information from those analyses is documented and communicated, to whom it is communicated, and how it is communicated; and
- reviewing the points at which the FDIC considers the cost effectiveness of PLCs.

To validate our understanding of the FDIC's methodology for determining costs associated with PLCs and whether the information the FDIC uses to make decisions was comprehensive, accurate, and timely and considered throughout the life cycle of the claim, we tested a non-statistical sample of PLCs related to four insured depository institutions that failed between 2008 and 2013. As illustrated in Table 3, below, our sampled institutions included those with (1) active PLC investigations, (2) PLCs closed after investigation without pursuing litigation, (3) active PLC mediation or litigation, (4) settled PLCs, as well as (5) institutions for which the PLC pursued multiple PLCs.

**Table 3: Summary of Sampled Institutions' PLCs**

Sampled Institution	Claims	Status			
		Active Investigation	Closed after Investigation	Mediation or Litigation	Settled
A	D&O Liability		✓		
	Accountant Malpractice		✓		
	Attorney Malpractice		✓		
	Fidelity Bond		✓		
	Appraiser Malpractice		✓		
B	D&O Liability		✓		
	Accountant Malpractice		✓		
	Attorney Malpractice		✓		
	Fidelity Bond		✓		
	Appraiser Malpractice		✓		
C	D&O Liability			✓	
	Accountant Malpractice	✓			
	Attorney Malpractice			✓	
	Fidelity Bond			✓	
	Appraiser Malpractice				✓
D	D&O Liability			✓	
	Accountant Malpractice		✓		
	Attorney Malpractice		✓		
	Fidelity Bond		✓		
<b>Total Claims</b>		<b>1</b>	<b>13</b>	<b>4</b>	<b>1</b>

Source: OIG Analysis of data from the PLU SharePoint site and DOLLARS.

## Objective, Scope, and Methodology

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For the claims related to the institutions in our sample, through access to the PLU (b)(5) (b)(5) (NFE), we:

- documented the chronology of events;
- collected and analyzed data, where applicable, for each phase of the PLCs;
- assessed the time it took for closing out claims;
- identified increases to the litigation budget, if applicable;
- reviewed IIC comments in (b)(5) and interviewed OAs to determine if OCs duplicated DRR Investigations's work;
- reviewed ongoing monitoring of claims;
- reviewed the completeness and our understanding of the information collected with both DRR Investigations and PLU staff; and
- discussed each case with the relevant OAs to confirm the process and documentation.

In addition, we interviewed the following FDIC officials to determine their roles, responsibilities, and perspectives related to this evaluation's objective:

- Director, DRR;
- Associate Director, Receivership Operations, DRR;
- Assistant Director, Investigations, DRR;
- DRR Resolution and Receivership Specialists;
- Acting Assistant General Counsel, Professional Liability and Financial Crimes Section, Legal Division;<sup>20</sup>
- Acting Senior Counsel, PLU;<sup>21</sup>
- PLU supervisory and senior counsel;

<sup>20</sup> Effective February 9, 2015, this individual reverted to her permanent position as Senior Counsel, PLU.

<sup>21</sup> Effective February 9, 2015, this individual reverted to her permanent position as Supervisory Counsel, PLU Group III.

## Objective, Scope, and Methodology

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- The Legal Division's Internal Control Liaison; and
- OAs for each institution in our sample.

## Glossary

Term	Definition
(b)(5)	
(b)(5)	



## Glossary

Term	Definition
SharePoint	A web application platform in the Microsoft Office server suite that allows users to store, track, and manage electronic documents.
Tort Claim	A civil legal claim, other than a breach of contract, for which a remedy may be obtained, usually in the form of damages.
(b)(5)	

## Acronyms and Abbreviations

Acronym / Abbreviation	Explanation
(b)(5)	
ATS	<i>Request for Authority to Sue</i>
D&O	Director and Officer
DMS	Data Management Services
(b)(5)	
DRR	Division of Resolutions and Receiverships
(b)(5)	
FRA	Federal Records Act
(b)(5)	
GAO	Government Accountability Office
IIC	Investigator-in-Charge
IT	Information Technology
(b)(5)	
OA	Oversight Attorney
OC	Outside Counsel
OIG	Office of Inspector General
PLC	Professional Liability Claim
PLU	Professional Liability Unit
RIM	Records and Information Management
RTC	Resolution Trust Corporation

## Corporation Comments



**Federal Deposit Insurance Corporation**  
550 17<sup>th</sup> Street, NW, Washington, DC 20429

February 10, 2016

**TO:** E. Marshall Gentry  
Assistant Inspector General for Evaluations  
Office of Inspector General

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

Charles Yi /*signed*/  
General Counsel

**SUBJECT:** Revised Management Response to Draft Office of Inspector General Evaluation Report Entitled, *The FDIC's Efforts to Ensure Professional Liability Claims are Cost Effective* (Assignment No. 2014-025)

Thank you for the opportunity to review and comment on the draft evaluation report by the Office of Inspector General ("OIG") for the Federal Deposit Insurance Corporation ("FDIC") entitled, *The FDIC's Efforts to Ensure Professional Liability Claims are Cost Effective* (Assignment No. 2014-025), dated December 4, 2015. The objective of the report is to evaluate the FDIC's efforts to maximize the cost-effectiveness of professional liability claims ("PLCs"). From 2008 through 2015, the period covered by the report, the FDIC recovered \$2.99 billion and incurred expenses of \$833.9 million. Since the inception of the PLC program in 1986, \$9.07 billion has been recovered with \$2.24 billion in expenses incurred. While the program has been cost-effective over the years, management of the Division of Resolutions and Receiverships ("DRR") and the Legal Division remain committed to making improvements wherever possible. Accordingly, the steps described following have been or will be taken with respect to each of the OIG's six recommendations. We understand that the report will not be made public and, because our response includes confidential or privileged information as well, it is provided with the understanding that it also will not be made public. We appreciate your review and recommendations.

**OIG Recommendation No. 1:** *To support enhanced coordination between DRR and the Legal Division, which would help ensure PLCs are cost effective, we recommend the DRR Director and the General Counsel:*

1. *Review, revise, and establish guidance that:*

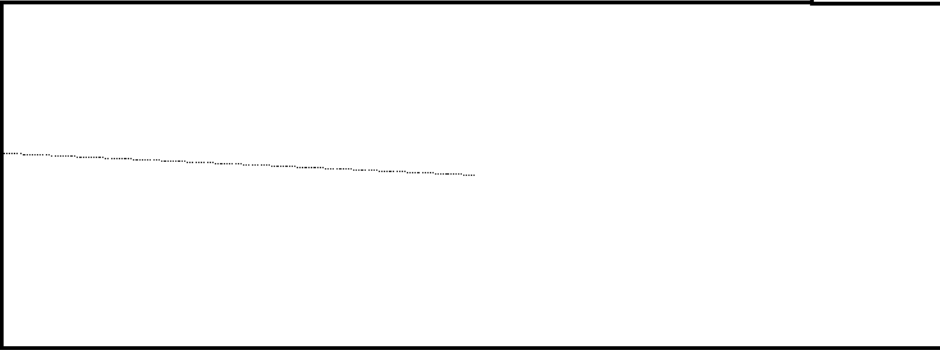
- *more clearly define DRR's and the Legal Division's respective roles and responsibilities to manage costs during the entire PLC life cycle;*

## Corporation Comments

- delineates PLC investigation scope to aid DRR and Legal Division staff in determining the extent of their respective investigative work;
- ensures each division's activities are communicated appropriately and coordinated throughout the PLC process, including allowing adequate opportunity to review and consider authority memorandums;
- supports timely closing PLC's that the FDIC determines lack merit, cost effectiveness, or both; and
- results in DRR and Legal Division expectations for coordination being consistent and complementary.

**Management Response:** DRR and Legal concur with this recommendation.

**Planned Corrective Action:** DRR and Legal will clarify their Divisions' respective roles and responsibilities and clearly communicate those roles and responsibilities to staff. DRR and Legal also will update their respective procedural manuals to incorporate this guidance. (b)(5)



**Proposed Implementation Date:** Completion of re-evaluation and manual updates: December 31, 2016.

**OIG Recommendation Nos. 2 & 3:** *To clarify how the FDIC determines and reassesses PLC cost effectiveness, we recommend the DRR Director and the General Counsel:*

2. Reassess the type of and extent to which costs related to the professional liability program are considered in determining whether a PLC is expected to be cost effective.
3. Review communications related to PLCs to ensure that program costs and costs considered in making cost effectiveness determinations are differentiated and presented clearly.

**Management Response:** DRR and Legal concur with both recommendations.

**Corrective Action Taken:** DRR and Legal historically have assessed all relevant costs in determining cost-effectiveness. All program expenses are regularly reported to the FDIC Board of Directors on a program-wide basis in PLC Annual Reports going back to the prior crisis. Costs for individual PLCs recommended to the Board or to delegated authority in authority-to-sue memoranda for approval are presented on a "going forward" basis only (i.e., "sunk" costs are

## Corporation Comments

not considered). This difference in considering and presenting costs has been integral to the proper management of the professional liability program from its inception in 1986. As a result, PLU already has procedures in place to make clear whether costs are being reported on a program-wide basis or are being considered only on a going forward basis as appropriate. In response to Recommendation 2, the DRR Director and the General Counsel have reconsidered these two methods of determining cost-effectiveness and have concluded that they remain fully appropriate. [REDACTED]

[REDACTED] During the course of its evaluation, the OIG concluded that it had found instances in which PLU's communications relating to PLC cost-effectiveness were not presented as clearly as they could have been – in particular in making cost-effectiveness assessments in authority-to-sue memoranda [REDACTED]

**Implementation Date:** Implemented as of December 16, 2015.

**OIG Recommendation No. 4:** *To clarify how the FDIC determines and reassesses PLC cost effectiveness, we recommend the DRR Director and the General Counsel:*

*4. Clarify at which key points in the life cycle of a case that FDIC should reassess cost effectiveness.*

**Management Response:** DRR and Legal concur with this recommendation.

**Planned Corrective Actions:** DRR and Legal have in place procedures to ensure that cost-effectiveness of a PLC is to be assessed [REDACTED]

**Proposed Implementation Date:** December 31, 2016.

**OIG Evaluation Recommendation No. 5:** *To ensure the FDIC appropriately documents the key decisions and the information used to make those decisions throughout the PLC process, we recommend the General Counsel:*

*5. Establish documentation expectations for PLCs and reflect such expectations in PLU procedures.*

## Corporation Comments

**Management Response:** Legal concurs with this recommendation.

PLU historically has documented key decisions and the information that supports those decisions

(b)(5)

(b)(5)

(b)(5)

In its evaluation report, the OIG observed that in one or more of the four failed institutions that it selected for evaluation in its review, the assigned OIA was not able to locate or could not readily locate one or more of the foregoing documents. PLU has improved its processes with the use of SharePoint since the four institutions at issue failed (the last of which failed in 2011) and will continue to rely on SharePoint for retention of key documents. PLU continues to work to improve its retention of complete copies of all of the foregoing documents for each failed institution by continuing to train staff regarding the importance of document retention. PLU is already documenting and will continue to document material reassessments of cost-effectiveness stated in the key documents noted previously.

(b)(5)

**Proposed Implementation Date:** Refresher training on SharePoint procedures will be provided to staff no later than January 31, 2016.

**OIG Recommendation No. 6:** *To ensure the FDIC appropriately documents the key decisions and the information used to make those decisions throughout the PLC process, we recommend the General Counsel:*

6. *Consider implementing an electronic case management system for the professional liability program to include a fully-searchable repository that maintains supporting case documentation.*

**Management Response:** Legal concurs with this recommendation.

**Corrective Actions Taken:** PLU currently maintains PLC-related documents electronically on [redacted] and on computer files of OAs, as well as in hard copy format – as the OIG evaluation report notes. This documentation is not as readily searchable or accessible as it could be if the Legal Division had a formal case management system similar to systems in use in the private sector (e.g., a system like iManage). Legal is currently limited to the technology that is available and accessible within the FDIC. Legal supports the implementation of a comprehensive document management system to the extent that budgetary and IT constraints permit. Such a system would provide an integrated system for use by case teams that would, among other things, provide one place for storage of all case specific communications (including email), allow teams to work more efficiently on a single draft document, create a repository that would allow for the efficient transition or retirement of files, and allow for differentiated access to documents within the repository to preserve confidences and privileges. However, Legal recognizes that these are corporation-wide systems and that a determination on the purchase and implementation of such a system requires approval outside Legal and DRR. Accordingly, at Legal's request, on January 29, 2016, the Legal

(b)(5)

## Corporation Comments

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Information Technology Unit requested that DIT authorize a business analysis related to the implementation of a document management system. In addition, [REDACTED]

(b)(5)

(b)(5)

## Summary of the Corporation's Corrective Actions

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

Rec. Number	Corrective Action: Taken or Planned	Expected Completion Date	Monetary Benefits	Resolved: <sup>a</sup> Yes or No	Open or Closed <sup>b</sup>
1	<p>DRR and the Legal Division will clarify their divisions' respective roles and responsibilities, clearly communicate those roles and responsibilities to staff, and update their respective [redacted] to incorporate such guidance. DRR and the Legal Division will implement a [redacted]</p>	December 31, 2016	\$0	Yes	Open
2	<p>DRR and the Legal Division historically have reported all program expenses to the FDIC Board of Directors in annual reports on the PLC program while presenting "going forward" expenses for individual PLCs. The DRR Director and the General Counsel have reconsidered these two methods of determining cost-effectiveness and have concluded that they remain fully appropriate. A [redacted]</p>	February 10, 2016	\$0	Yes	Closed
3	<p>The Legal Division added an explicit statement in authority memoranda that [redacted]</p>	December 16, 2015	\$0	Yes	Closed



## Summary of the Corporation's Corrective Actions

Rec. Number	Corrective Action: Taken or Planned	Expected Completion Date	Monetary Benefits	Resolved: <sup>a</sup> Yes or No	Open or Closed <sup>b</sup>
4	<p>DRR and the Legal Division will clarify in their respective [redacted] existing procedures to ensure that cost effectiveness of a PLC is to [redacted]</p>	December 31, 2016	\$0	Yes	Open
5	PLU will continue efforts to improve its retention of complete copies of all of the foregoing documents for each failed institution and provided refresher SharePoint training to its staff.	January 31, 2016	\$0	Yes	Closed
6	The Legal Division supports the implementation of a comprehensive document management system to the extent that budgetary and IT constraints permit. However, the Legal Division recognizes that these are corporation-wide systems and that a determination on the purchase and implementation of such a system requires approval outside Legal and DRR. Accordingly, the Legal Division requested that DIT authorize a business analysis related to the implementation of a document management system.	January 29, 2016	\$0	Yes	Closed

<sup>a</sup> Resolved – (1) Management concurs with the recommendation, and the planned, ongoing, and completed corrective action is consistent with the recommendation.

(2) Management does not concur with the recommendation, but alternative action meets the intent of the recommendation.

(3) Management agrees to the OIG monetary benefits, or a different amount, or no (\$0) amount. Monetary benefits are considered resolved as long as management provides an amount.

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



# Office of Inspector General

Office of Audits and Evaluations  
Report No. AUD-14-006

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## The FDIC's Receivership Basic Ordering Agreements for Business Process Operations Services

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information and is for official use only.  
Other than the Executive Summary,  
the contents of the report are not  
releasable without the approval of the  
Office of Inspector General.**

March 2014

# Office of Inspector General

## Executive Summary

### The FDIC's Receivership Basic Ordering Agreements for Business Process Operations Services

Report No. AUD-14-006  
March 2014

#### Why We Did The Audit

When an insured financial institution fails, the FDIC is appointed receiver by the primary chartering authority. The FDIC, in its receivership capacity, through the Division of Resolutions and Receiverships (DRR), manages the assets of a failed bank to preserve or enhance their value and disposes of them as quickly as possible. The FDIC uses a number of information technology (IT) applications to facilitate the management, marketing, and servicing of assets, and has relied heavily on the use of contractors and failed bank staff to carry out its receivership obligations, including outsourcing Business Process Operations (BPO) services. The work covered by BPO contractors covers pre-closing, closing, and post-closing activities involved in a failed bank's closure.

On April 22, 2010, the FDIC executed Receivership Basic Ordering Agreements (RBOA) for BPO services, one to Fiserv Federal Systems, Inc. (Fiserv) (RECVR-10-G-0079) and the other to Fidelity National Information Services, Inc. (Fidelity) (RECVR-10-G-0080). As of early February 2014, the FDIC had awarded 280 Task Orders (TO) totaling \$190,930,363 to Fiserv and 230 TOs for a total value of \$166,862,204 to Fidelity under their respective RBOAs.

The primary objective of this audit was to determine whether payments made by the FDIC to Fiserv and Fidelity were adequately supported, allowable under the terms of the contracts, and reasonable. In addition, we performed work related to TOs awarded by the FDIC to Fiserv (TO 0071) and Fidelity (TO 0060) for implementing a toolkit called [REDACTED] to be used in converting failed bank information from a bank's data processing system into the FDIC's systems. The purpose of our work was to determine whether (1) contractor tasks and deliverables were within the scope of the task order statements of work (SOW) and (2) associated billings were reasonable.

To achieve our objective, we tested simple random samples of the labor and travel cost universes under these RBOAs that the FDIC paid Fiserv and Fidelity in 2012. In regard to the [REDACTED] TOs, we (b)(5) discussed the scope of work within the TOs with DOA and DRR officials, analyzed the two TOs, tested labor and travel transactions, and relied on the work from a separate OIG Audit, *The FDIC's Controls over Business Unit-Led Application Development Activities*, Report No. AUD-13-007, issued September 11, 2013. In addition, we performed data analyses on the labor and travel cost universes under both RBOAs for the period April 22, 2010 through February 14, 2013 to identify trends, inconsistencies, and anomalies in labor and/or travel costs billed to the FDIC.

#### Background

An RBOA is used to expedite the acquisition of goods and/or services in support of failing or failed institutions and is similar to a Basic Ordering Agreement (BOA) except it is limited to awards in support of DRR and is not assigned a monetary value or a contract ceiling. Rather, dollar value ceiling controls are established at the TO level, allowing DRR the ability to formulate requirements and resultant cost estimates as needs become better defined. DRR uses the RBOA vehicle for obtaining various services such as receivership assistance, loan servicing and collections, asset valuations, and BPO.

## Executive Summary

# The FDIC's Receivership Basic Ordering Agreements for Business Process Operations Services

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The services provided by BPO contractors Fiserv and Fidelity included but were not limited to:

- Determining the data processing environment and IT operation activities prior to closing;
- Downloading data during pre-closing activities;
- Regulating and controlling the data processing, communication systems, e-banking, wire transfers, Web sites, and other applications at bank closing;
- Converting bank general ledger data for transfer to FDIC systems;
- Coordinating with the acquiring institution to transfer operations of the bank after closing;
- Providing IT support to the FDIC;
- Providing forensic support for the investigations function; and
- Providing interim servicing for retained loans.

In addition, the FDIC awarded 13 nonbank-specific TOs to Fiserv and 12 to Fidelity under their respective RBOAs for services related to areas such as Training, 4-C System Administration, Loss Share, Job Aids, Deposit Downloads, Post-Closing Direct Support, Post-Closing Indirect Support, Large Bank Modernization, Weekly Reporting, Large Bank Simulation, and Settlement and Release of Claims.

## Audit Results

DRR has established and implemented various control activities for overseeing Fiserv and Fidelity to help ensure that the contractors meet their respective performance objectives and comply with contract provisions. DRR developed and issued the *Division of Resolutions and Receiverships Contract Oversight Manual* (DRR COM) to provide a daily operating guide for contract oversight staff in the performance of their contract oversight responsibilities. DRR also has a robust invoice review process, including weekly meetings with Fiserv and Fidelity to discuss labor charges and monthly meetings to discuss travel charges, to help ensure that contractor claims for labor and travel costs under the BPO RBOAs are appropriate and supportable.

To test the adequacy of these controls, we reviewed simple random samples of 280 Fiserv and Fidelity labor and travel cost charges incurred during 2012 (December 2012 travel expense information was not available at the time of our review for Fidelity). We verified labor charges against the price schedule in the contract and qualifications in contractor employee resumes. We verified travel charges against supporting travel receipts and government lodging and per diem rates. We found no exceptions. Accordingly, we can estimate with a confidence level of 95 percent that labor and travel charges incurred by Fiserv in 2012, labor charges incurred by Fidelity during 2012, and travel charges incurred by Fidelity during the period January through November 2012 were adequately supported and consistent with rates approved in the task orders with an error rate of at most 3.8 percent. As part of our testing, we also verified the contract deliverable that the FDIC received for each sampled labor charge. For certain labor charges, we had to rely on explanations provided by DRR rather than reviewing source documents. In regard to evaluating the reasonableness of charges associated with the [REDACTED] TOs, 17 of the 280 (b)(5) charges we tested were expenses incurred while performing work under the [REDACTED] TOs, and we (b)(5) concluded that these charges were reasonable. In addition, we judgmentally selected labor charges under (b)(5) the [REDACTED] TOs and concluded that these charges were reasonable.

**Executive Summary****The FDIC's Receivership Basic Ordering  
Agreements for Business Process Operations  
Services**Report No. AUD-14-006  
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During the course of our audit, we became aware of contract actions and unanticipated funding increases that illustrate a need for greater DRR and DOA coordination when planning for program needs that will involve contractors.

Finally, in performing analyses of the labor and travel costs universes, we identified instances where contractor employees in travel status are not always using hotel tax exemption forms when incurring lodging expenses in any of the 11 states that offer the exemption for hotel occupancy taxes. We are referring this matter to DRR and DOA for further study because it may provide an opportunity to reduce contractor travel expenses in these and other FDIC contracts.

The report contains four recommendations intended to strengthen controls for monitoring the performance of BPO contractors that cover pre-closing, closing, and post-closing activities for failed banks and enhancing acquisition team coordination. In addition, we included an observation for management's attention and further study related to contractor employees using hotel occupancy tax exemption forms when incurring expenses in any of the states that offer exemptions.

**Corporation Comments**

On March 26, 2014, the Director, DOA, and the Director, DRR, provided a joint written response to a draft of this report. In the response, the Director, DOA, concurred with recommendations 1 and 2, which are addressed to DOA and DRR, and the Director, DRR, concurred with all four of the report's recommendations, which are addressed to DRR. The response described ongoing and planned actions to address the recommendations. DOA and DRR intend to complete planned actions by December 31, 2014.

Because this report contains sensitive information, we do not intend to make the report available to the public in its entirety. We will, however, post this Executive Summary on our public Web site.

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

Office of Audits and Evaluations  
Office of Inspector General

**DATE:** March 31, 2014

**MEMORANDUM TO:** Arleas Upton Kea, Director  
Division of Administration  
  
Bret D. Edwards, Director  
Division of Resolutions and Receiverships

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

**SUBJECT:** *The FDIC's Receivership Basic Ordering Agreements for  
Business Process Operations Services*  
(Report No. AUD-14-006)

This report presents the results of our audit of the FDIC's Receivership Basic Ordering Agreements (RBOA) for Business Process Operations (BPO) services with Fiserv Federal Systems, Inc. (Fiserv) (RECVR-10-G-0079) and Fidelity National Information Services, Inc. (Fidelity) (RECVR-10-G-0080). The FDIC executed both RBOAs on April 22, 2010, and as of early February 2014, the FDIC awarded 280 Task Orders (TO) totaling \$190,930,363 to Fiserv and 230 TOs for a total value of \$166,862,204 to Fidelity under their respective RBOAs.

The primary objective of this audit was to determine whether payments made by the FDIC to Fiserv and Fidelity were adequately supported, allowable under the terms of the contracts, and reasonable. In addition, we performed work related to TOs awarded by the FDIC to Fiserv (TO 0071) and Fidelity (TO 0060) for implementing a toolkit called (b)(5) [redacted] to be used in converting failed bank information from a bank's data processing system into the FDIC's systems. The purpose of our work was to determine whether (1) contractor tasks and deliverables were within the scope of the task order statements of work (SOW) and (2) associated billings were reasonable.

To address our objective, we (1) reviewed policies, procedures, and control processes for awarding and administering the BPO contracts with Fiserv and Fidelity and for overseeing contractor performance; (2) interviewed Division of Resolutions and Receiverships (DRR) program officials and Division of Administration (DOA) contracting officials responsible for these BPO contracts; and (3) tested simple random samples of the labor and travel cost universes under these RBOAs that the FDIC paid (b)(5) Fiserv and Fidelity in 2012. In regard to the [redacted] TOs, we discussed the scope of work within the TOs with DOA and DRR officials, analyzed the TOs, tested select labor (b)(5) and travel charges attributable to [redacted] work, and relied on the work from a

separate FDIC OIG audit, *The FDIC's Controls over Business Unit-Led Application Development Activities*, Report No. AUD-13-007 issued in September 2013.

We also reviewed selected additional TOs and performed data analysis of Fiserv and Fidelity labor and travel expenses for reasonableness and to identify anomalies.

We conducted this performance audit in accordance with generally accepted government auditing standards. Appendix 1 of this report includes additional details on our objective, scope, and methodology; Appendix 2 provides a detailed description of our statistical sampling methodology; Appendix 3 contains the Corporation's comments on this report; and Appendix 4 contains a summary of the Corporation's corrective actions.

## Background

An RBOA is used to expedite the acquisition of goods and/or services in support of failing or failed institutions and is similar to a Basic Ordering Agreement (BOA) except it is limited to awards in support of DRR and is not assigned a monetary value or a contract ceiling. Rather, dollar value ceiling controls are established at the TO level, allowing DRR the ability to formulate requirements and resultant cost estimates as needs become better defined. DRR uses the RBOA vehicle for obtaining various services such as receivership assistance, loan servicing and collections, asset valuations, and BPO.

The services provided by BPO contractors Fiserv and Fidelity included but were not limited to:

- Determining the data processing environment and information technology (IT) operation activities prior to closing;
- Downloading data during pre-closing activities;
- Regulating and controlling the data processing, communication systems, e-banking, wire transfers, Web sites, and other applications at bank closing;
- Converting bank general ledger data for transfer to FDIC systems;
- Coordinating with the acquiring institution to transfer operations of the bank after closing;
- Providing IT support to the FDIC;
- Providing forensic support for the DRR investigations function; and
- Providing interim servicing for retained loans.

As of early February 2014, the FDIC had awarded 267 bank-specific and 13 nonbank-specific TOs to Fiserv and 218 bank-specific and 12 nonbank-specific TOs to Fidelity under their respective RBOAs. The FDIC awarded individual bank-specific TOs for each failed institution. The FDIC awarded nonbank-specific TOs for services related to areas



such as Training, 4-C System<sup>1</sup> Administration, Loss Share, Job Aids, Deposit Downloads, Post-Closing Direct Support, Post-Closing Indirect Support, Large Bank Modernization, Weekly Reporting, Large Bank Simulation, and Settlement and Release of Claims.

Under the RBOAs, Fiserv and Fidelity provided IT support leading up to the institution failure (pre-closing), during closing weekend, and during the receivership processes (post-closing). The FDIC purchased InfoSphere from the IBM Corporation to be used in converting information from the failed bank's data processing system into the FDIC's systems. In October 2010, the FDIC awarded TO 0071 and TO 0060 to Fiserv and Fidelity, respectively, to support the implementation of InfoSphere and development of procedures and processes related to its use.

DOA and DRR collectively manage the contract award and administration process. DOA is responsible for entering into and administering contracts, ensuring compliance with terms of the contracts, and protecting the interests of the FDIC in all of its contractual relationships. DRR is responsible for overseeing the day-to-day work, reviewing and approving deliverables and contract invoices, and informing DOA of any needed changes to the contract. DOA's Acquisition Services Branch (ASB) officials in Dallas managed the contracting aspects of these RBOAs while DRR Dallas officials in Contract Oversight provided oversight management of the contracts.

## Audit Results

DRR has established and implemented various control activities for overseeing Fiserv and Fidelity to help ensure that the contractors meet their respective performance objectives and comply with contract provisions. To test the adequacy of these controls, we reviewed simple random samples of Fiserv and Fidelity (1) labor charges against the contract price schedule and qualifications in contractor employee resumes and (2) travel charges against supporting travel receipts and government lodging and per diem rates. Based on our results, we concluded that labor and travel payments made to Fiserv and Fidelity under the BPO RBOAs during 2012 were adequately supported, consistent with the rates approved in the TOs, and reasonable. In regard to evaluating the reasonableness of charges associated with the [REDACTED] TOs, 17 of the 280 charges we tested were expenses incurred while performing work under the [REDACTED] TOs, and we concluded that these charges were reasonable. In addition, we judgmentally selected labor charges under the [REDACTED] TOs and concluded that these charges were reasonable.

During the course of our audit, we became aware that DRR and DOA had different views as to whether tasks assigned by DRR to Fiserv and/or Fidelity were within the scope of the RBOAs or associated TOs. These instances involved the [REDACTED] TOs and other TOs and required unanticipated funding increases and unplanned modifications. We

<sup>1</sup> 4-C is DRR's system of record for failed bank assets retained in receiverships.

(b)(5) noted that DRR did not always prepare, and ASB did not always require, justifications for the funding increases for the [REDACTED] TOs. In addition, DOA and DRR agreed to (b)(5) ratify Fidelity's [REDACTED] TO in order to resolve confusion and uncertainty regarding the use of an unauthorized subcontractor that had not been approved by the CO, as required by the APM. These actions illustrate a need for greater DRR and DOA coordination when planning for program needs that will involve contractors.

## DRR's BPO Contract Oversight Process

DRR has established various control activities for overseeing Fiserv and Fidelity to help ensure that the contractors meet their respective performance objectives and comply with contract provisions. DRR developed and issued the *Division of Resolutions and Receiverships Contract Oversight Manual* (DRR COM) to provide a daily operating guide for contract oversight staff in performing their contract oversight responsibilities. DRR also has a robust invoice review process, as described below, to help ensure that Fiserv's and Fidelity's claims for labor and travel costs under the BPO RBOAs are appropriate and supportable.

DRR uses Oversight Managers (OM), Task Order Oversight Managers (TOOM), and Technical Monitors (TM) to monitor the performance of its contractors. The DRR COM provides that DRR contract oversight staff work closely with ASB in implementing ASB's *Acquisition Policy Manual* (APM) and *Acquisition Procedures, Guidance and Information* (PGI), which supplements the APM. The APM and PGI represent the FDIC's official policies, procedures, and guidance for all FDIC contracts.

OMs, TOOMs, and TMs are responsible for ensuring the timeliness and accuracy of invoices received from DRR contractors, and only substantiated amounts are paid for completed work. DRR established a comprehensive billings review and payment approval process for the BPO contracts with Fiserv and Fidelity, which includes:

- reviewing invoices, contractor weekly labor charges spreadsheets, contractor monthly travel charges spreadsheets, time sheets, travel vouchers, and supporting documentation;
- preparing weekly reports outlining topics, concerns, and documents contract oversight staff want to discuss and address at weekly meetings with the contractors;
- verifying invoices against spreadsheets updated to address questions and concerns raised by contract oversight staff;
- reviewing travel data files against labor hours, travel and accommodation rates, and travel receipts;
- ensuring that all travel issues are reconciled and reflected in the monthly travel invoices; and
- meeting with Fiserv and Fidelity weekly to review labor reports and monthly to review travel reports and address any questions.

### **BPO Labor Costs**

The RBOAs are, for the most part, time and materials contracts. Using a spreadsheet containing labor hour charges for calendar year 2012, we randomly selected 140 labor charges for detailed testing—70 for Fiserv and 70 for Fidelity. In testing the 140 labor charges, we performed the following:

- Reviewed resumes to determine whether the contractor employees providing the services had the appropriate experience to work and provide the required deliverables.
- Verified that Fiserv and Fidelity submitted invoices reflecting and supporting the labor hours billed to the FDIC.
- Confirmed that the labor categories agreed with the labor category prices documented in the RBOAs and respective TOs.
- Recalculated the amounts billed to verify their accuracy.
- Worked with DRR to identify contract deliverables resulting from the labor charges.

We determined that Fiserv's and Fidelity's labor costs paid by the FDIC for the 140 tested charges were adequately supported, consistent with the rates approved in the task orders, and reasonable. Accordingly, we can estimate with a confidence level of 95 percent that Fiserv and Fidelity labor expenses during 2012 were adequately supported and consistent with rates approved in the task orders with an error rate of at most 3.8 percent. When practical, we were able to associate the labor charges with specific deliverables, such as pre-closing data request tracking (DRT) reports, screen prints depicting standard reports, files showing data downloads from closed banks to FDIC internal systems, forensics reports, bank collateral file data reports, and accounting reports. We verified that the deliverables were associated with the correct institution and that the timing of the labor charge was reasonable in relation to the deliverable date. However, for certain charges, such as those associated with servicing loans or managing projects, we relied on DRR's assurances that the work performed was satisfactory. In those instances, loan servicing files were too voluminous or there were no single documents that could be attributed to the sampled and tested project management labor charges.

### **BPO Travel Costs**

Fiserv and Fidelity employees also incur travel expenses in carrying out their RBOA duties. Both contractors maintain master spreadsheets containing all travel costs. Again, we selected a random sample of 140 travel charges for detailed testing—70 for Fiserv and 70 for Fidelity. In testing the travel charges, we performed the following:

- Determined whether the travel expenses were incurred during the scope of the contracted services identified in the respective TOs.
- Verified the reasonableness of the travel destinations in relation to the locations where the work was performed.

- Confirmed that Fiserv and Fidelity provided receipts to support the billed amounts.
- Verified that hotel rates were appropriate for the locations and that government lodging rates were obtained.
- Determined the reasonableness and sufficiency of documentation provided to support taxicab, tolls, baggage handling, and miscellaneous expenses.

We determined that Fiserv's and Fidelity's travel costs paid by the FDIC for the 140 tested charges were adequately supported, consistent with the rates approved in the task orders, and reasonable. Accordingly, we can estimate with a confidence level of 95 percent that Fiserv travel expenses during 2012 and Fidelity travel expenses from January through November 2012 were adequately supported and consistent with rates approved in the task orders with an error rate of at most 3.8 percent.

### **Data Analytics**

We also performed some routine data analysis of the labor and travel databases to confirm that billed costs appeared reasonable. For the labor database, we performed various sorts and subtotals to ensure the following:

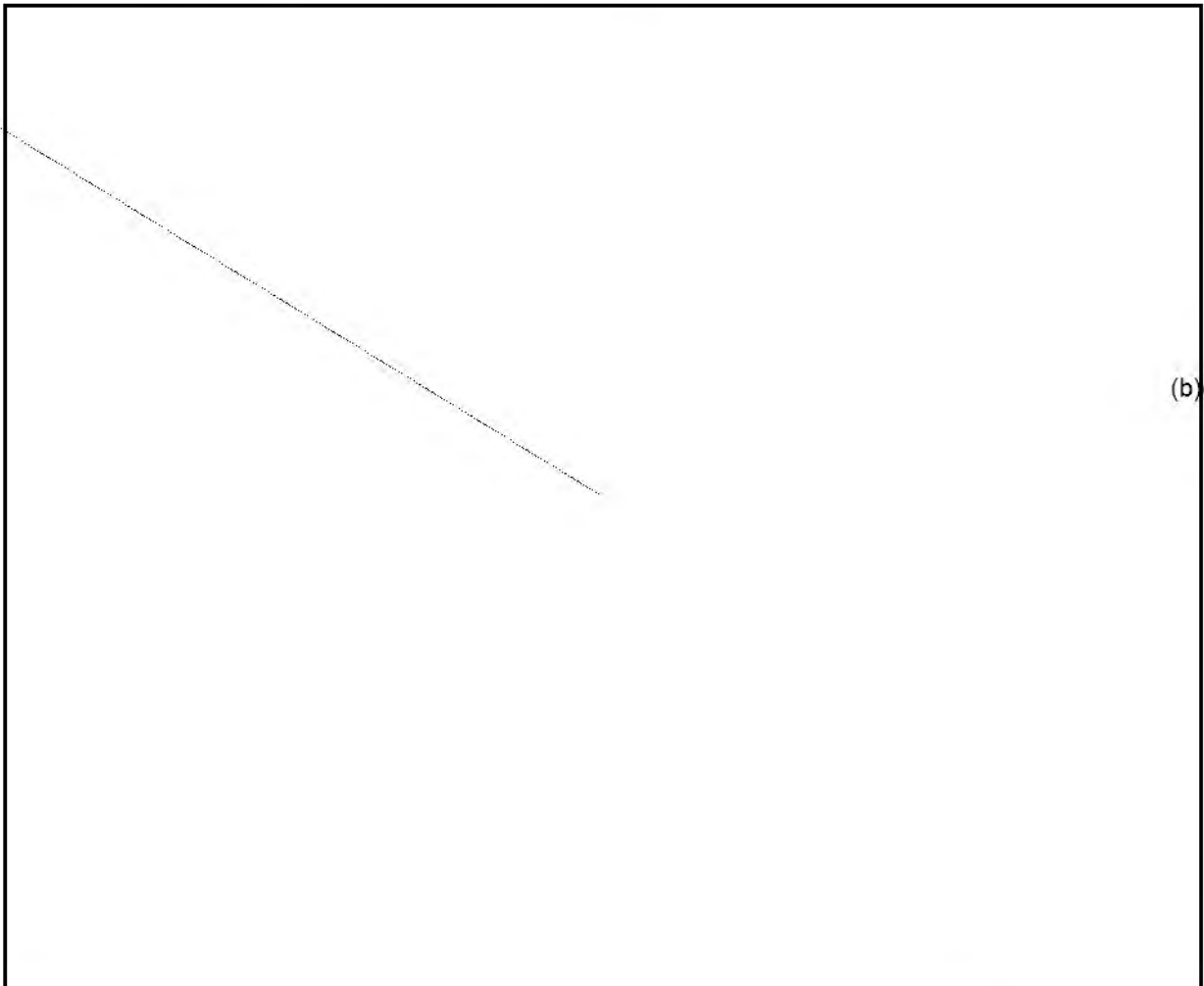
- Labor categories were billed consistently in agreement with the price schedule.
- Selected employees were billed at the same labor category throughout the contract.
- Employees did not bill excessive hours of labor in a single day.
- There were no instances of duplicate employees.

For the travel database, we confirmed that certain expenses, such as taxi fares, were reasonable, and per diem amounts agreed with General Services Administration (GSA) rates.

### **Contracting Actions Illustrate a Need for Greater DOA and DRR Coordination**

During the course of our audit, we became aware that DRR and DOA had different views as to whether tasks assigned by DRR to Fiserv and/or Fidelity were within the scope of the RBOAs or associated TOs. These instances involved [REDACTED] and other (b)(5) TOs and required unanticipated funding increases and unplanned modifications. We noted that DRR did not always prepare, and ASB did not always require, justifications for the funding increases for [REDACTED] TOs. In addition, DOA and DRR agreed to ratify Fidelity's InfoSphere TO in order to resolve confusion and uncertainty regarding the use of an unauthorized subcontractor that had not been approved by the CO, as required by the APM. These actions illustrate a need for greater DRR and DOA coordination when planning for program needs that will involve contractors.

(b)(5) [redacted] **Application Development Efforts:** For our review of the [redacted] TOs, (b)(5) we determined that some of the IT tasks performed by Fiserv and Fidelity, as well as the resulting deliverables, were application development activities in nature that were not explicitly addressed in the RBOA scope of services or the InfoSphere TO SOW. As discussed earlier, these TOs instructed Fiserv and Fidelity to support the implementation of the [redacted] software and to develop procedures and processes related to the use of (b)(5) [redacted]. The TOs defined [redacted] as a toolkit purchased by the FDIC to be used (b)(5) in the data transformation process from a bank's data processing system into FDIC systems. However, DRR also used these TOs to perform application development work (b)(5) using Oracle's [redacted] facility, system maintenance services, and associated stakeholder reports for the following eight IT software projects:



DRR indicated that a June 2011 modification expanded the SOW to include the [redacted] (b)(5) application development activities. This modification revised the RBOA and [redacted] (b)(5) TOs to add three new labor categories, two of which were [redacted] Programming Specialist (b)(5) and Senior [redacted] Programming Specialist. Section IV, Labor Categories, of the RBOA (b)(5) stated that:

(b)(5) [T]he [redacted] will document and assist in the design and development of procedures and processes using the Oracle [redacted] development toolkit, web technologies and other programs in the resolution of institutions and manipulation of financial data for reporting and analysis with direction from the Oversight Manager or Technical Monitor. The [redacted] (b)(5)  
 (b)(5) [redacted] will develop various reports for the use of the BIS stakeholders. The [redacted] (b)(5)  
 (b)(5) [redacted] will model, discover, map, and analyze data across multiple information sources, and automate information integration across multiple FDIC applications.

(b)(5) However, Section II of the RBOA, Scope of Services, and the [redacted] SOW did not mention [redacted] or application development work. (b)(5)

In April 2013, DRR requested that DOA issue separate TOs under the BPO RBOAs for the eight applications in order to better track application development costs. DOA informed DRR that this software development work was outside the scope of the BPO RBOAs and DOA would not be able to issue the TOs requested by DRR. Instead, DOA stated that a new contract would need to be developed to address the application development work. DRR responded that much of the application development work for these eight applications had been completed and that soliciting and issuing a new contract would significantly delay completion of the eight applications, but disagreed that the work was out of scope. In order to facilitate a more defined process going forward, DOA and DRR agreed to complete the application development work for the eight applications under the Infosphere TOs, but required that any future application development work be completed under the new contract.

(b)(5) Table 1 on the next page presents information about expense modifications to the [redacted]. As illustrated, these application development efforts described above resulted in significant cost increases to the TOs.

**Table 1: InfoSphere TOs and Modifications Related to Expenditure Ceilings and Periods of Performance**

TO and Modification (MOD)	Fiserv Dollars	Fiserv Period of Performance	Fidelity Dollars	Fidelity Period of Performance
TO awarded 10/19/2010			\$2,699,320	1 year: 10/19/2011
TO awarded 10/20/2010	\$2,699,320	1 year: 10/20/2011		
MOD #6 executed 01/26/2012	N/A	N/A	Increased to \$4,499,320	N/A
MOD #6 executed 04/20/2012	Increased to \$4,459,320	N/A	N/A	N/A
MOD #9 executed 08/28/2012	Increased to \$7,627,320	Extended to 10/19/2013	N/A	N/A
MOD #10 executed 08/28/2012	N/A	N/A	Increased to \$6,659,320	N/A
MOD #12 executed 05/08/2013	Increased to \$8,127,320*	N/A	N/A	N/A
MOD #14 executed 05/22/2013	Increased to \$9,667,320	N/A	N/A	N/A
MOD #15 executed 10/04/2013	Increased to \$11,423,139	Extended to 12/31/2013	N/A	N/A
MOD #16 executed 12/16/2013	N/A	Extended to 01/31/2014	N/A	N/A
MOD #16 executed 01/06/2014.	N/A	N/A	N/A	Extended to 02/28/2014

Source: OIG Review of DOA's Consolidated Document Information System (CDIS).

Note: Administrative contract modifications and certain modifications extending periods of performance are not presented in Table 1.

\* The \$500,000 additional funding was for [redacted] work only because [redacted] had been stopped for a brief period of time (May 8-14, 2013).

We noted that DRR did not always prepare, and ASB did not always require, justifications for the funding increases noted in Table 1. The APM and PGI provide that prior to awarding a contract modification that increases the total value of a contract, the CO and OM must ensure that any funding and approvals have been obtained and the necessary documentation, including a Justification for Non-Competitive Procurement (JNCP)—required when a funding increase exceeds 15 percent of the original award amount—has been entered into the official contract file. In regard to the Fiserv [redacted] TO, a JNCP was prepared for the funding increase in Modification 15 executed on October 4, 2013, but there were no JNCPs for the other TO modifications (#s 6, 9, 10, and 14). Although the JNCP prepared for TO Modification #15 included a discussion of the other non-competitive TO modifications for funding increases, these modifications had been executed 5 to 18 months prior to Modification 15 – long after the timeframe stipulated in the APM and PGI.



DRR provided information showing that a former CO [REDACTED] told the (b)(6) DRR OM that a JNCP would not be required for Modification #9, executed in August 2012 for a funding increase of \$3,168,000. ASB could not readily explain why a JNCP was not required, but noted that all contract actions are situational. ASB noted that it would typically require a JNCP for any funding increase greater than 15 percent of the original award amount.

(b)(5) In regard to the Fidelity [REDACTED] TO, we did not locate any JNCPs for the funding increases in Modifications 6 and 10 in the official contract file.

DRR has RBOA Implementation Procedures, dated December 31, 2008, that include guidance for identifying contracting needs, preparing funding requisitions, and processing RBOAs and TOs; conducting on-site management of TOs; and overseeing RBOAs. However, the procedures are silent on funding and JNCP requirements for TO modifications. We also noted that the RBOA Implementation Procedures do not mention desired coordination and communication activities between the DRR OMs and TMs and the ASB COs and Contract Specialists.

(b)(5) Technically, the labor category description in the June 2011 modification to the RBOA contemplates process design using the [REDACTED] tool kit to manipulate failed bank financial data for reporting and analysis purposes which could be interpreted as application development activities. However, given the fact that the contract ceiling quadrupled for Fiserv and more than doubled for Fidelity, we would expect to see more explicit contract language within the RBOA Scope of Services section and/or the [REDACTED] SOW (b)(5) defining the nature of the application development work, contract requirements, and associated deliverables. We would also expect to see greater justification for the non-competitive cost increases.

We recommend that DRR and DOA reiterate to DRR and ASB staff the APM requirement for written justifications for contract extension and funding increases, including JNCPs. We decided not to make recommendations specifically related to

(b)(5) [REDACTED] because:

(b)(5) (1) Fiserv and Fidelity completed their [REDACTED] work, and DRR is in the process

(b)(5) of closing out the [REDACTED] TOs.

(2) DRR and DOA initiated activities to award a contract for services related to applications, including development, maintenance, optimization, and other related functions under a different BOA not associated with the Fiserv or Fidelity RBOA.

(3) In response to a recommendation made in a prior OIG report regarding mitigating risks associated with business unit-led application development,<sup>2</sup> the FDIC agreed to include language in a planned corporate policy on business unit-led application

<sup>2</sup> OIG Report No. AUD-13-007, *The FDIC's Controls over Business Unit-Led Application Development Activities*, dated September 11, 2013.



development that requires FDIC business units to coordinate with the FDIC's Division of Information Technology (DIT) to ensure that applications developed by business units are recorded in the Corporation's information systems inventory, when appropriate, and develop written IT governance processes that address the review and approval of developed proposals, the decision-making process for authorizing the deployment of applications to the production environment, and the tracking and reporting of application development costs. The FDIC issued Circular 1300.7, *Information Technology Development Policy*, on January 30, 2014.

(b)(5) We noted that DRR and DIT have a Memorandum of Understanding (MOU), dated December 6, 2010, regarding the use of [REDACTED] by DRR to support emerging business and information requirements. DIT and DRR were in the process of revising this MOU, but at the time of our draft report, the revised and updated MOU had not yet been executed. We recommended that DRR work with DIT to expedite the signing and execution of the revised MOU, especially in light of the new DRR application development BOA discussed above. DRR agreed with the intent of the recommendation but took an alternative action as discussed in the Corporation Comments and OIG Evaluation section of this report.

We identified several other situations involving an unauthorized [REDACTED] subcontractor and potential out-of-scope work associated with other TOs where there was a lack of coordination and agreement between DRR and DOA. We provided the details of those situations, including the risks and effects, separately to DRR and DOA. (b)(5)

### **Mitigating Risks Through Closer Coordination and Up-Front Planning**

When administering a contract, it is important to ensure that all assigned contractor tasks and deliverables are clearly covered by the existing contract statement of work. Any action that causes the contractor to extend or expand the requirements of the contract and thus impact the price, schedule, quantities or quality of the deliverables, or change other substantive terms and conditions of the contract beyond the SOW may be considered an unauthorized contractual commitment. OMs and COs must be aware of, and guard against, the potential of unauthorized contractual commitments and proactively coordinate any events that could result in such an action. Determining how to address procurement needs that do not fit squarely within an existing contract requires the joint involvement of the program and contracting office. To that end, the DRR COM states that DRR's Contract Oversight Department should work closely with ASB and is an integral part of the contracting process to ensure compliance with technical aspects of a contract while fulfilling the mission of the FDIC.

While only one of the issues we identified resulted in contract ratification, there were several actions where it appeared ASB conceded to allow work to continue and process certain contract actions without further documentation and approvals in order to avoid negatively impacting DRR operations. In each case, DRR and ASB could have

benefitted from better up-front planning and coordination. It is incumbent on the program office, in these instances DRR, to involve ASB officials as early as possible in situations where its business needs and requirements must be addressed through contracting activities. It is also incumbent on ASB to protect the FDIC's interests by ensuring that, ultimately, all requirements of the APM and applicable law, regulations, and other applicable procedures and approvals have been met. We recognize that some of our findings may have been better understood and accepted during the financial crisis because of the unprecedented volume of work required under very tight timeframes. However, the pace of bank failures has declined significantly since 2010, and the contracting actions we are citing in this report occurred, for the most part, during 2012 and 2013 – subsequent to the crisis.

### **Recommendations**

We recommend that the Director, DRR, and Director, DOA:

- (1) Reiterate to DRR and ASB staff the requirement for written justifications for contract extension and funding increases, including written JNCs when funding increases exceed 15 percent of the original award amount.
- (2) Reemphasize to appropriate DRR and ASB personnel the importance of coordinating contracting activities and requirements among the program, contract oversight, and contracting officials.

We recommend that the Director, DRR:

- (3) Coordinate with the Director, DIT, to finalize, sign, and execute the Memorandum of Understanding regarding the use of

(b)(6) [Redacted]

[Redacted]

(b)(5)

- (4) Revise and issue RBOA Implementation Procedures to include a section that establishes expectations for timely, frequent, and open coordination among COs, OMs, and TOOMs and written justifications for TO modifications for funding increases and period of performance extensions.

### **Observation – Hotel Tax Exemptions**

In performing analyses of the labor and travel charges, we identified instances where contractor employees in travel status are not always using hotel tax exemption forms when incurring lodging expenses in those states that offer the exemption for hotel occupancy taxes. Eleven states provide exemptions from sales and/or occupancy taxes on hotels/motels for government employees on official travel – Alaska, Delaware, Florida, Kansas, Massachusetts, Missouri, New York, Oregon, Pennsylvania, Texas, and Wisconsin. The FDIC's Division of Finance (DOF) Web site contains the appropriate state tax exemption forms to be completed and submitted to lodging establishments.

When contractors purchase goods or services to use in performance of an FDIC contract, they generally have to pay the taxes assessed on the goods or services because contractors cannot claim tax-exempt status by virtue of the fact that they are performing work for the FDIC. However, some jurisdictions may extend the FDIC tax-exemption to contractors, depending on the nature of the charge. In that event, DOA APM and PGI tax procedures suggest that contractors should take advantage of all available exemptions. The FDIC's Contractor Travel Reimbursement Guidelines do not specifically mention hotel tax exemptions. DRR's travel guidelines for Fiserv and Fidelity state that hotel taxes are reimbursable, even though some contractors are able to secure tax exemptions from certain hotels.

In reviewing the travel universe databases for Fiserv and Fidelity BPO RBOAs, we identified thousands of incidents of hotel tax charges. Fiserv and Fidelity travel databases do not separately break-out federal and state taxes so we could not readily quantify amounts attributable to federal and state lodging tax expense. We are referring this matter to DRR and DOA for further study because it may provide an opportunity to reduce contractor travel expenses in these and other FDIC contracts.

## Corporation Comments and OIG Evaluation

The Director, DOA, and the Director, DRR, provided a joint written response, dated March 26, 2014, to a draft of this report. The response is presented in its entirety in Appendix 3. In the response, the Director, DOA, concurred with recommendations 1 and 2, which are addressed to DOA and DRR, and the Director, DRR, concurred with all four of the report's recommendations, which are addressed to DRR. In addition, the response describes completed and planned corrective actions to address the recommendations. DOA and DRR intend to complete planned actions by December 31, 2014.

(b)(5) With respect to recommendation 3, which related to finalizing, signing, and executing the MOU regarding the use of Oracle's [REDACTED] DRR responded that the MOU had been superseded by Circular 1300.7, *Information Technology Development Policy*, dated January 30, 2014. DRR noted that Circular 1300.7 is intended to be a corporate-wide policy defining governance structures for addressing FDIC information technology development, deployment, and maintenance activities, which include the use of APEX. The issuance of Circular 1300.7 meets the intent of our recommendation and we consider recommendation 3 to be closed.

(b)(5) A summary of the Corporation's corrective actions is presented in Appendix 4. The completed or planned actions are responsive to the recommendations, and the recommendations are resolved. Recommendations 1, 2, and 4 will remain open until corrective action has been completed.

## Objective, Scope, and Methodology

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### Objective

The primary objective of this audit was to determine whether payments made by the FDIC to Fiserv Federal Systems, Inc. (Fiserv) and Fidelity National Information Services, Inc. (Fidelity) under their respective Receivership Basic Ordering Agreements (RBOA) for Business Process Operations (BPO) services were adequately supported, allowable under the terms of the contracts, and reasonable. In addition, we performed work related to TOs awarded by the FDIC to Fiserv (TO 0071) and Fidelity (TO 0060) for implementing a toolkit called [REDACTED] to be used in converting failed bank information from a bank's data processing system into the FDIC's systems. The purpose of our work was to determine whether (1) contractor tasks and deliverables were within the scope of the task order statements of work (SOW) and (2) associated billings were reasonable.

We conducted this performance audit from April 2013 to January 2014 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

### Scope and Methodology

The scope of this audit included Fiserv and Fidelity RBOA and TO contract activities from April 2010 (date of both RBOA awards) through mid-February 2013. We also reviewed contract activity from April 2010 through mid-January 2014 for the InfoSphere and select other TOs (i.e., Job Aids, DMS, and DINB/BOC). To achieve the objectives, we performed the following procedures and techniques.

(1) Reviewed policies, procedures, and control processes for awarding and administering the BPO contracts with Fiserv and Fidelity and for overseeing contractor performance, including:

- *FDIC Acquisition Policy Manual*, dated August 22, 2008.
- *Acquisition Procedures, Guidance and Information (PGI) Manual*, dated March 2011.
- *Division of Resolutions and Receiverships Contract Oversight Manual*, dated December 2011.
- *DRR Contract Oversight Procedural Memorandum (OM-11-009), Invoice Review/Payment and Invoice Credit Procedure*, dated March 25, 2011.
- *DRR Receivership Basic Ordering Agreement (RBOA) Implementation Procedures*, dated December 31, 2008.
- *DRR Asset Resolution Manual*, dated May 9, 2011.
- *FDIC Failed Financial Institution Closing Manual*, dated April 22, 2010.

- Circular 3700.16, *DRR Contract Management*, dated January 17, 2008.
- *DRR Resolutions Manual*, dated March 28, 2011.
- *DRR/DIT Memorandum of Understanding for* [REDACTED] (b)(5)
- [REDACTED] dated December 6, 2010.
- *FDIC Contractor Travel Reimbursement Guidelines* and the United States General Services Administration nightly lodging allowances.

- (2) Reviewed the Fiserv and Fidelity BPO RBOAs and bank-specific and nonbank-specific TOs included in our sample of labor and travel charges.
- (3) Interviewed DRR contract oversight and program officials and DOA contracting officials responsible for the Fiserv and Fidelity BPO RBOAs to identify and obtain an understanding of (a) the Corporation's established internal controls related to contracting and contractor oversight and (b) the RBOAs and associated TOs.
- (4) Tested a statistically valid selection of the labor and travel costs universes under the BPO RBOAs that the FDIC paid Fiserv and Fidelity during 2012.<sup>3</sup> See Appendix 2 for details on the statistical sampling methodology.

(b)(5) (5) In regard to the [REDACTED] TOs, we discussed the scope of work within the TOs with DOA and DRR officials, analyzed the TOs, tested select labor and travel charges attributable to [REDACTED] work, and relied on the work from a separate FDIC OIG audit, *The FDIC's Controls over Business Unit-Led Application Development Activities*, Report No. AUD-13-007 issued in September 2013.

- (6) In regard to the other TOs (Job Aids, DMS, and DINB/BOC), we discussed the scope of work with DRR and DOA officials and analyzed aspects of the TOs.

We performed our work at the FDIC's offices in Arlington, Virginia.

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

As described in the Scope and Methodology section of this Appendix, we performed audit procedures to identify and obtain an understanding of the FDIC's established internal controls related to contracting and contractor oversight. However, consistent with the stated objective, we did not assess the implementation or effectiveness of those controls or the adequacy of the FDIC's overall internal control or management control structure beyond what we include in this report. We obtained data from DRR's information systems and DOA's Consolidated Document Information System (CDIS); however, we did not assess the effectiveness of information system controls.

With any contract of the size and scope of the Fiserv and Fidelity RBOAs, there is increased risk that contractors could inappropriately bill the FDIC for additional hours or

<sup>3</sup> December 2012 travel charges were not available for Fidelity at the time that we selected our sample.

improperly allocate contract charges to the wrong task order and that such charges could go undetected by the program office or our audit. However, DRR's oversight efforts and controls help mitigate that risk, and we designed our audit procedures to provide reasonable assurance that billings are adequately supported and allowable.

The Government Performance and Results Act of 1993 (the Results Act), as amended, directs Executive Branch agencies to develop a customer-focused strategic plan, align agency programs and activities with concrete missions and goals, and prepare and report on annual performance plans. For this audit, we did not assess the strengths and weaknesses of the FDIC's annual performance plan in meeting the requirements of the Results Act because such an assessment is not part of the audit objectives. The FDIC's compliance with the Results Act is reviewed in program audits of FDIC's operations.

Regarding compliance with laws and regulations, as part of our testing of labor and travel charges, we included steps to determine whether the FDIC, Fiserv, and Fidelity had complied with provisions of the APM, the BPO RBOAs, and respective TOs. The results of our tests are discussed, where appropriate, in the report. Additionally, we assessed the risk of fraud and abuse related to our objectives in the course of evaluating audit evidence.



## Statistical Sampling Methodology

### Sample Universe

The universe for this audit was all Fiserv and Fidelity labor and travel expenditure charges incurred during the period April 22, 2010 (RBOAs award date) through mid-February 2013. We identified those charges from data provided to us by DRR's Business Information Systems (BIS) and Contract Oversight organizations in the Dallas Regional Office, which downloaded four databases - Fiserv travel, Fiserv labor, Fidelity travel, and Fidelity labor. DRR provided the data in four Microsoft Excel files.

The audit universe provided by DRR consisted of the following:

- (b)(4) • **Fiserv Travel** [ ] charges incurred during the period 05/02/2010 – 01/26/2013.
- (b)(4) • **Fiserv Labor** [ ] charges incurred during the period 04/26/2010 – 02/22/2013.
- (b)(4) • **Fidelity Travel** [ ] charges incurred during the period 04/25/2010 – 02/28/2013.
- (b)(4) • **Fidelity Labor** [ ] charges incurred during the period 04/26/2010 – 02/22/2013.

We sampled Fiserv travel and labor charges included in the databases for 2012. We sampled Fidelity travel charges included in the database for the period January-November 2012 and labor charges for 2012. The 2012 database charges consisted of the following:

- (b)(4) • **Fiserv Travel** [ ] charges incurred during 2012.
- (b)(4) • **Fiserv Labor** [ ] charges incurred during 2012.
- (b)(4) • **Fidelity Travel** [ ] charges incurred during the period January-November 2012.
- (b)(4) • **Fidelity Labor** [ ] charges incurred during 2012.

Using random numbers, we selected a total of 280 charges—70 from each of the databases—for detailed testing.

### Sample Design and Size

We consulted with the FDIC Division of Insurance and Research (DIR) Data Applications Section to determine a minimum sample size to ensure sufficiently precise estimation. We used a sample size of 70 records for each of the four databases – Fiserv travel and labor and Fidelity travel and labor. This ensured that finding no errors in the sample for any particular database would mean that the universe error rate was less than four percent with 95 percent confidence.

DIR generated random numbers for each of the samples – Fiserv travel and labor and Fidelity labor and travel. DIR determined that if there are no errors found in a simple random sample of 70 line items (charges), the proportion of line items (charges) with errors in the population is at most 3.8 percent.

### **Characteristics Measured**

In testing the travel charges, we verified the following:

- Travel occurred during the scope of the contracted services.
- Travel destination was reasonable in relation to the work performed.
- Documentation was provided to support the expense incurred.
- Mileage expenses were reasonable.
- Hotel rates appeared appropriate for the location.
- Per diem rates claimed agreed with the approved government rates.
- Taxi, airfare, and rental car charges appeared reasonable.

In testing the labor charges, we verified the following:

- Labor rates billed were consistent with the contracting pricing schedules.
- Fiserv and/or Fidelity employees met the requisite labor qualifications (determined by a review of employees' resumes).
- Contractors provided the requisite deliverables resulting from labor charges.



# Corporation Comments



**Federal Deposit Insurance Corporation**  
3601 Fairfax Drive, Arlington, VA 22226

Division of Administration

**DATE:** March 26, 2014

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

**FROM:** Arleas Upton Kea, Director [REDACTED] (b)(6)  
Division of Administration  
Bret D. Edwards, Director [REDACTED] (b)(4)  
Division of Resolutions and Receiverships

**SUBJECT:** Management Response to the Draft OIG Audit Report Entitled,  
*The FDIC's Receivership Basic Ordering Agreements for Business  
Process Operations Services* (Assignment No. 2013-025)

This is in response to the subject draft Office of Inspector General (OIG) audit report, issued February 27, 2014. In its report, the OIG made four recommendations two recommendations jointly to the Division of Resolutions and Receiverships (DRR) and the Division of Administration (DOA) and two recommendations to DRR.

We appreciate the review performed by the OIG. In its report, the OIG noted that there are various oversight control activities in place to ensure that the contractors' performance objectives are met. However, we recognize the need to address certain issues identified by the OIG. This response outlines the planned corrective actions for each recommendation cited in the OIG's report.

## MANAGEMENT DECISION

**Recommendation 1 (DRR and DOA):** Reiterate to DRR and DOA Acquisition Services Branch (ASB) staff the requirement for written justifications for contract extension and funding increases, including written Justification for Non-Competitive Procurement (JNCP) when funding increases exceed 15 percent of the original award amount.

**DRR and DOA Management Response:** DRR and DOA concur with this recommendation.

### Corrective Action:

DRR: DOA's current Oversight Management Certification Program includes training that emphasizes the requirements for written justifications for contract extensions, funding increases, including funding increases that exceed 15 percent of the original award value. DRR expects this training program to be completed for the existing applicable staff in 2014. Additionally, DRR conducts internal Oversight Management training where these requirements will be emphasized.

## Corporation Comments

DOA: DOA ASB Policy & Systems Section will send an email to ASB Contracting Officers to reiterate the requirement for written justifications for contract extension and funding increases, including written JNCs when funding increases exceed 15 percent of the original award amount. DOA ASB will also share the email with the DRR Dallas Contract Oversight Group.

**Completion date:**

DRR will complete its proposed actions by December 31, 2014.

DOA ASB will issue an email by April 30, 2014.

**Recommendation 2 (DRR and DOA):** Reemphasize to appropriate DRR and DOA ASB personnel the importance of coordinating contracting activities and requirements among the program, contract oversight, and contracting officials.

**DRR and DOA Management Response:** DRR and DOA concur with this recommendation.

**Corrective Action:**

DRR: DOA ASB and DRR staff participate in several regularly scheduled meetings where these topics will be discussed and emphasized. We will ensure that the Oversight Management Certification training and DRR Contract Oversight training place emphasis on the importance of this coordination. Additionally, by April 30, 2014, we will issue an email to Oversight Managers stressing the importance of coordinating contracting activities and requirements among the program, contract oversight, and contracting officials.

DOA: DOA ASB will issue an email to ASB Contracting Officers to emphasize the importance of coordinating contracting activities and requirements among program office and ASB personnel (Oversight Managers and Contracting Officers). DOA ASB will share such email with the DRR Dallas Contract Oversight Group. The responsibilities and expectations for communicating contract activities is also a subject that is addressed in detail as part of the FDIC's Oversight Manager training courses, which FDIC Oversight Managers are required to complete as part of the FDIC's Oversight Management Certification Program. Emphasis on this subject will continue to be made in the FDIC OM Courses.

**Completion Date:**

DRR will issue an email by April 30, 2014.

DOA ASB will issue an email by April 30, 2014.

**Recommendation 3 (DRR):** Coordinate with the Director, DIT, to finalize, sign, and execute the Memorandum of Understanding regarding the use of Oracle's [REDACTED] by DRR.

(b)(5)

**DRR Management Response:** DRR agrees with the intent of this recommendation. Refer to the alternate solution as noted in the corrective action section.

## Corporation Comments

**Corrective Action:**

(b)(5) The December 6, 2010, MOU that provided specific guidance for DRR's use of [REDACTED] (b)(5)  
[REDACTED] has been superseded by Circular 1300.7, issued by the FDIC's Acting CIO on  
January 30, 2014. This Circular is intended to be a corporate-wide policy defining governance  
structures for addressing FDIC information technology development, deployment, and  
(b)(5) maintenance activities, which include the use of [REDACTED] as well as other tools that may be used  
by the FDIC, regardless of which Division or Office is doing the development.

**Completion Date:** Completed January 30, 2014.

**Recommendation 4 (DRR):** Revise and issue RBOA Implementation Procedures to include a section that establishes expectations for timely, frequent, and open coordination among COs, OMs, and Task Order Oversight Managers (TOOMs) and written justifications for TO modifications for funding increases and period-of-performance extensions.

**DRR Management Response:** DRR concurs with this recommendation.

**Corrective Action:**

DRR will review the current Job Aids applicable to Contract Oversight to ensure that these expectations are clearly incorporated. These Job Aids will be referenced and linked on the FDIC intranet.

**Completion Date:** December 31, 2014.

## Summary of the Corporation's Corrective Actions

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

Rec. No.	Corrective Action: Taken or Planned	Expected Completion Date	Monetary Benefits	Resolved: <sup>a</sup> Yes or No	Open or Closed <sup>b</sup>
1	<b><u>DRR's Response:</u></b> DRR expects to provide Oversight Management Certification Program training to existing applicable staff in 2014. This training emphasizes the requirements for written justifications for contract extensions and funding increases, including funding increases that exceed 15 percent of the original award value. Additionally, DRR conducts internal Oversight Management training where these requirements will be emphasized.	DRR 12/31/2014	\$0	Yes	Open
	<b><u>DOA's Response:</u></b> DOA ASB Policy & Systems Section will send an email to ASB Contracting Officers to reiterate the requirement for written justifications for contract extension and funding increases, including written JNCPs, when funding increases exceed 15 percent of the original award amount. DOA ASB will share the email with the DRR Dallas Contract Oversight Group.	DOA 4/30/2014	\$0	Yes	Open
2	<b><u>DRR's Response:</u></b> DOA ASB and DRR staff will participate in several regularly scheduled meetings where these topics will be	DRR 4/30/2014	\$0	Yes	Open

Rec. No.	Corrective Action: Taken or Planned	Expected Completion Date	Monetary Benefits	Resolved: <sup>a</sup> Yes or No	Open or Closed <sup>b</sup>
	<p>discussed and emphasized. DRR will ensure that the Oversight Management Certification training and DRR Contract Oversight training place emphasis on the importance of coordination. DRR will also issue an email to Oversight Managers stressing the importance of coordinating contracting activities and requirements among the program, contract oversight, and contracting officials.</p> <p><b><u>DOA's Response:</u></b> DOA ASB will issue an email to Contracting Officers to emphasize the importance of coordinating contracting activities and requirements among program office and ASB personnel (Oversight Managers and Contracting Officers). DOA ASB will share the email with the DRR Dallas Contract Oversight Group. DOA noted that the FDIC's Oversight Manager training courses, which FDIC Oversight Managers are required to complete as part of the FDIC's Oversight Management Certification Program, address the responsibilities and expectations for communicating contract activities in detail. DOA will continue to emphasize this subject in the FDIC OM Courses.</p>	DOA 4/30/2014	\$0	Yes	Open
3	The December 6, 2010 MOU that provided specific guidance for DRR's use of	Completed 1/30/2014	\$0	Yes	Closed

Rec. No.	Corrective Action: Taken or Planned	Expected Completion Date	Monetary Benefits	Resolved: <sup>a</sup> Yes or No	Open or Closed <sup>b</sup>
(b)(5)	<div style="border: 1px solid black; height: 1.2em; width: 100%;"></div> <p>was superseded by Circular 1300.7, issued by the FDIC's Acting CIO on January 30, 2014. This circular is intended to be a corporate-wide policy defining governance structures for addressing FDIC information technology development, deployment, and maintenance activities, which include the use of <span style="border: 1px solid black; display: inline-block; width: 1.2em; height: 1.2em; vertical-align: middle;"></span> as well as other tools that may be used by the FDIC, regardless of which Division or Office is performing the development.</p>				
(b)(5)					
4	DRR will review the current Job Aids applicable to Contract Oversight to ensure that coordination expectations are clearly incorporated. DRR will reference and link these Job Aids on the FDIC intranet.	12/31/2014	\$0	Yes	Open

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

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