

**General Government Division**

B-254081

December 4, 1992

The Honorable John Glenn  
Chairman, Committee on  
Governmental Affairs  
United States Senate



148215

Dear Mr. Chairman:

You asked for an update on the results of our work on the Western Storm project since the March 3, 1992, hearing before your Committee. Specifically, you asked that we provide an overall assessment of the project, discuss Resolution Trust Corporation's (RTC) efforts to correct its contracting deficiencies, and provide the results of our inquiry into alleged criminal conduct and certain other matters relating to the award and performance of the Western Storm contract.

Overall, the results of our work validated our preliminary findings presented to the Committee at the March hearing. As a result we continue to believe that (1) the Western Storm project was poorly planned, (2) inappropriate contracting tools were employed, (3) limited oversight was provided, and (4) the government's interests were not adequately protected. However, while RTC has made some changes to improve internal controls over its contracting process, certain other changes seem to have increased their vulnerability to fraud, waste, and abuse. Furthermore, we did not uncover any evidence of criminal conduct in the award or performance of the Western Storm contract.

**BACKGROUND**

The Western Storm Project was created to reconcile the asset records of 92 failed thrifts with RTC's general ledger. A \$24 million contract was awarded to the Financial Management Task Force (FMTF) on April 2, 1991, to complete this work. Shortly after work began, questions developed concerning the contract award process and the quality of work performed by the contractor. On

March 3, 1992, we presented our preliminary findings on the review of the project to the Committee.<sup>1</sup> Our review showed that (1) the contract had been improperly issued, (2) written justification and approvals required for a noncompetitive award were not obtained by headquarters officials from the RTC Board prior to issuing the task orders to FMTF, (3) RTC regional officials failed to request legal advice on the appropriateness of the procurement procedure used, and (4) a contractor representative had been involved in 3 days of preaward discussion with RTC officials.

Since then, other congressional committees asked that we examine various issues related to Western Storm. On April 27, 1992, the Senate Committee on Banking, Housing, and Urban Affairs requested that we review RTC's examination of FMTF's fitness and integrity certification. Additionally, we testified on August 6, 1992, before the House Committee on Banking, Finance and Urban Affairs, Subcommittee on General Oversight and Investigations, on Western Storm and efforts to correct RTC's contracting deficiencies.<sup>2</sup>

#### APPROACH

To complete this work, we examined RTC and contractor records and reviewed reports on Western Storm issued by RTC's Inspector General<sup>3</sup> and an independent auditor hired by RTC. We also interviewed contractor and RTC officials who worked on this project and reviewed RTC's revised Contract Policies and Procedures Manual. In looking for evidence of possible wrongdoing, we examined general journal entries; cash disbursements with related supporting documentation; bank, payroll, and tax records at FMTF and Yale & Seffinger, an FMTF subcontractor. We were unable to complete our review of contractor records until late June 1992 because of delays in obtaining access to those records. We also reviewed a transcript of the March 3, 1992, hearing and statements given to us during our interviews.

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<sup>1</sup>Resolution Trust Corporation: Preliminary Results of Western Storm Investigation and Related Contracting Deficiencies (GAO/T-OSI-92-5, Mar. 3, 1992) and (GAO/T-GGD-92-16, Mar. 3, 1992)

<sup>2</sup>Resolution Trust Corporation: Western Storm and Related Contracting Deficiencies (GAO/T-GGD-92-67, Aug. 6, 1992).

<sup>3</sup>Western Region's Asset Stratification and Reconciliation Project, (A92-007), February 24, 1992; and Oversight of Baird, Kurtz & Dobson's Audit of the Western Region's Reconciliation and Asset Re-Stratification Project, Oversight Report OS92-002, April 15, 1992.

We did our follow-up work from March through August 1992 in accordance with generally accepted government auditing standards.

CONTRACTING WEAKNESSES  
LED TO WESTERN STORM

Overall, we believe that RTC's mindset undervalued contracting, even though RTC extensively used private sector contractors to accomplish its mission. This mindset led to fundamental weaknesses in RTC's contracting system and permitted Western Storm to occur. Poor planning, poor oversight at both the regional and headquarters levels, and use of an improper contracting vehicle in the Western Region created an unmanageable project. RTC has improved its contracting system, but some weaknesses remain.

The following chronology illustrates key events leading up to the initiation of the Western Storm project:

November 2, 1990

The former RTC Executive Director tells the RTC Board that he will send all sole source professional services contracts for more than \$50,000 to the RTC Board as required by RTC procedures.

April 1991

RTC's Assistant General Counsel for Contracting learns from an RTC Western Regional Office attorney that a \$20 million sole source contract has been issued for Western Storm without the review and approval of RTC Counsel. The Assistant General Counsel discusses the project with RTC's former Executive Director and the Director of Contracting.

April 25, 1991

RTC's Director of Contracting is asked to determine the circumstances relating to the issuance of the Western Storm task orders. His inquiry finds that in his opinion, the 92 task orders were clearly a case of "order splitting" to avoid higher level approval within RTC.

May 2, 1991

RTC's former Executive Director and other headquarters officials hold a telephone conference with Western Region officials on whether the Western Storm project was within established RTC policies. The project was allowed to continue. Headquarters management did not

schedule follow-up monitoring for the project, nor were the task orders brought to the attention of the RTC Board.

#### December 1991

Following the start of our investigation, RTC's Senior Vice President initiates an investigation into Western Storm at the request of RTC's Chief Executive Officer.

#### SOME ACTIONS TAKEN TO IMPROVE CONTRACTING

Since your March 1992 hearing, improvements have been made to some internal controls over RTC's contracting system. In May 1992, RTC revised its contracting manual. Generally, the revisions clarified the responsibilities of various offices and expanded the description of specific aspects of the RTC system. For example, RTC expanded the section on the use of task order agreements, clarified its delegations of authority to issue contracts, and established the Contracting Officer Warranting Program. Under this program, only certain authorized contracting officers may sign contracts obligating RTC, thus reducing the possibility that RTC staff unfamiliar with contracting system requirements will award contracts.

Subsequent to revising its contracting manual, RTC made two major changes intended to improve internal controls and address our concerns. First, RTC created three headquarters positions with responsibility for ensuring field contracting office compliance with RTC policies and procedures. RTC introduced the competition advocate program to help promote fair and adequate competition. These are positive steps, but since these steps are new, we cannot determine their effectiveness at this time.

#### ADDITIONAL IMPROVEMENTS NEEDED

While some of the problems that allowed the Western Storm project to occur have been corrected, changes to other sections of the revised contracting manual seem to have increased RTC's vulnerability to fraud, waste, and abuse. In response to RTC staff criticisms about the prior system's ability to meet their needs for timely issuance of contracts, the revised manual provides wide discretion for staff at several critical and sensitive points in the system. For example, rather than requiring competitive bidding to renew contracts, RTC's revised contracting manual gives its staff discretion to noncompetitively renew existing contracts. Other sections give RTC staff discretion in choosing who may bid for a contract and in determining the extent and manner in which negotiations will be conducted.

In addition, we remain concerned that RTC management does not have an information system to monitor compliance with its contracting policies and procedures. RTC's Contracting Activity Reporting System only provides an inventory of contract solicitations and issued contracts. It does not, for example, identify the extent that and circumstances under which noncompetitive contracting procedures are used, nor does it serve as a management tool for comparing payments with amounts authorized for each contract.

#### ETHICS EXAMINATION FOLLOWED REGULATIONS

In addition to reviewing the contracting system changes, we reviewed RTC's compliance with its ethics requirements in examining FMTF employees' fitness and integrity certifications. RTC regulations<sup>4</sup> have been issued that implement the statutory requirement that contractors meet minimum standards for fitness and integrity. Contractors self-certify that they meet the minimum requirements, and in many circumstances before contract award RTC is to verify the contractor's certification and/or any other related information it deems necessary.

We found that RTC complied with its procedures as they relate to fitness and integrity examinations of FMTF officers.<sup>5</sup> Although certain management officials did have ties to failed institutions, these ties themselves did not disqualify the officers from doing business with RTC. No financial regulatory agency has determined that these officials engaged in activities --such as causing a substantial loss to the failed institution-- that would have required their disqualification.

#### NO EVIDENCE OF CRIMINAL CONDUCT IN CONTRACT AWARD OR PERFORMANCE

After the March 3, 1992, hearing we completed our inquiry into alleged criminal conduct by examining the books and records of FMTF and Yale & Seffinger. From this work, we found no evidence of criminal conduct in the award or performance of the contract for the Western Storm project.

As requested, we also reviewed the testimony by RTC officials at the March hearing. At that hearing, we testified that RTC held meetings over the weekend of March 15, 1991, in order to plan the Western Storm project. We also stated that these meetings were

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<sup>4</sup>"Qualification of, Ethical Standards of Conduct for, and Restrictions on the use of Confidential Information by Independent Contractors." 12 C.F.R. part 1606

<sup>5</sup>Review of RTC Fitness and Integrity Certifications for Western Storm (GAO/GGD-92-31R, Sept. 23, 1992).

attended by a partner of Yale & Seffinger, who at one time had been a member of the Board of Directors of FMTF.

In a June 19, 1992, interview with our staff, the Yale & Seffinger partner told us that the weekend meetings were held for the purpose of discussing Western Storm. He also said that he attended the meetings in order to discuss the project.

At the March hearing, RTC's Western Storm Project Director was asked why the Yale & Seffinger partner was present during the weekend planning meetings. The Project Director testified that the "contractor was present because of his responsibilities in the Central Processing Center" (p. 72, lines 18 to 20 of the hearing transcript), and that he was "on-site" because of these CPC responsibilities (p. 85, lines 6 to 8). When asked why the Yale & Seffinger partner was there instead of a representative from competing accounting firms, the Project Director responded that "he was there solely from his responsibilities under performance of the CPC contract" (p. 86, lines 24 and 25; p. 87, line 1).

The Project Director did not further explain why the partner's experience under the existing CPC contract was relevant to the discussions that took place on the Western Storm project. More importantly, he did not make it clear that the partner actively participated in discussions about the Western Storm project. This was important in light of the subsequent award of the Western Storm contract to FMTF, which engaged Yale & Seffinger as a subcontractor on the project.

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As agreed with the Committee, unless you publicly release its contents earlier, we plan no further distribution of this letter until 30 days from the date of issuance. At that time, we will send copies of this letter to the Ranking Minority Member of the Senate Committee on Governmental Affairs, the Chief Executive Officer of the RTC, the Chairman of the Thrift Depositor Protection Oversight Board, and other interested parties. Copies

will also be made available to others upon request. If you have any questions regarding this correspondence, please call me at (202) 736-0479.

Sincerely yours,



Gaston L. Gianni, Jr.  
Associate Director,  
Federal Management Issues

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7

GAO/GGD-93-8R, RTC Western Storm Follow-up