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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON REGIONAL OFFICE
FIFTH FLOOR
803 WEST BROAD STREET
FALLS CHURCH, VIRGINIA 22046

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OCT 18 1973

Mr. Richard Platt, Jr.
Acting Director
Federal Savings and Loan
Insurance Corporation
101 Indiana Avenue, NW.
Washington, D.C. 20552

Dear Mr. Platt:

The General Accounting Office has completed its examination of the financial activities of the Corporation's Midwestern Office (MWO) for the year ended December 31, 1972. We have treated this work in arriving at our opinion on the Corporation's annual financial statements which are in our report to the Congress, dated August 31, 1973 (B-114827).

As you know, our Chicago Office suggested several improvements in accounting procedures at MWO while work was underway. These matters were discussed in greater detail with Mr. Stuckwisch and the MWO staff upon the completion of the audit. We are enclosing for your information a summary of these items.

A factor which we believe underlies the problems discussed in the enclosure is the lack at MWD of an up-to-date accounting manual. In discussing this with your associates, they thought it would be useful for us to summarize for your consideration our thoughts on the benefits of an accounting manual. A manual of accounting policies and procedures is an important part of a sound internal control system and it contributes to accurate and reliable accounting and operating data. A clear definition of the procedures by which individual responsibilities should be fulfilled can result in a more efficient operation.

A manual would greatly assist in day-to-day operations and ensure that accounting, budgetary, and related records are properly maintained. The manual should establish the policies and procedures necessary for prompt, accurate, and consistent recording of accounting transactions, periodic reconciliation and review of subsidiary and general ledger accounts, and control over documents and records.

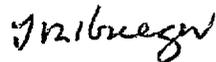
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We believe an accounting manual would contribute to an improved internal control system and would minimize accounting problems, such as those discussed in the enclosure. Corporation officials agreed that an accounting manual is needed and its development is being considered.

We would appreciate receiving your comments on any actions taken or planned on this matter. We would also like to express our appreciation for the cooperation and assistance furnished us during our examination.

Sincerely yours,



H. L. Krieger
Regional Manager

Enclosure

DETAILED INFORMATION ON THE RESULTS OF GAO'S
FINANCIAL EXAMINATION AS OF DECEMBER 31, 1972
MIDWESTERN OFFICE
FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

ACCOUNT BALANCES

The balances of several accounts were misstated because accounting transactions were not recorded promptly and accurately.

| <u>Account</u> | <u>Description of activity</u> | <u>Account balance at 12/31/72</u> |
|----------------|-------------------------------------|--|
| 1013 | Loans in Foreclosure | \$13,447,641 |
| 1313 | Real Estate Contracts in Forfeiture | 360,475 |
| 1330 | Real Estate in Judgement | 836,581 |

We took a statistical random sample of individual items in these accounts for confirmation with the attorneys handling the legal matters. Out of 152 confirmations, attorneys returned six exceptions which disclosed that properties valued at almost \$81,000 were improperly included in Acct. 1013. In addition, the value of nonincome-producing properties in a vacant and vandalized condition are included in the above accounts, but MWO officials were not certain to what extent. Similar properties are also recorded in Acct. 1901 - Mortgages on properties to be demolished.

| | | |
|------|------------------------------|---------|
| 1925 | Accounts Receivable - Motels | 327,480 |
|------|------------------------------|---------|

The account was overstated by more than \$266,000 because the receivables were not charged off when the motels were sold in the years 1969, 1970, and 1972. Officials stated this was an oversight, and took corrective action in March 1973 to correct the account.

| | | |
|------|--|--------|
| 1960 | Accounts Receivable - Beverly Safe Deposit Corp. | 25,992 |
|------|--|--------|

The assets represented by this account were sold in 1970 for cash of \$3,500 and a note of \$6,500. The accounting department was not aware of the sale until February 1973, at which time corrective action was taken to remove this account from the books.

| <u>Account</u> | <u>Description of activity (contd.)</u> | |
|----------------|---|----------------|
| 2660 | Deferred Interest Income | \$ 125,585 CR. |
| 3101 | Interest on Mortgage Loans | 1,001,342 CR. |

Account 2660 was overstated by almost \$22,000 because transactions were not posted at regular intervals. Likewise, interest on mortgage loans was understated by the same amount.

| | | |
|------|--|-------------|
| 2350 | Accounts Payable (one of six accounts that make up MWO's complete accounts payable amount) | 392,059 CR. |
|------|--|-------------|

The subsidiary ledgers supporting the accounts payable were more than \$100,000 greater than the balance. MWO officials told us that attempts to reconcile the records have never been completed. In addition, we noted that accounts payable is debited for the payment of attorney bills before the liability is recorded in the account, and that in two cases we examined, more than a month elapsed before the liability was posted to the account. Notwithstanding the unreconciled amount, the account balance at any given statement date cannot be accurate because of this accounting practice. MWO officials stated that they are trying to reduce the time it takes to record the liabilities and pay the bills.

INACTIVE ACCOUNT AND
OUTSTANDING CHECKS

The MWO has no policy or procedure for reviewing balances of inactive accounts or canceling payment of checks which are outstanding for a long period. As a result, we noted the following.

1. Account 1716 - Deferred Charges - Other. The account has been \$846 since 1968 with no offsetting credits. The detail records are in storage and MWO officials were not certain of the nature of the charges. They said that the account will be written off because of its age and inactivity.

2. Account 1520 - Cash. The account included amounts for 12 outstanding checks dated between 1969 and January 1972 which had not been presented for payment by December 31, 1972. One check for \$650 was paid in January 1973, and the remaining 11 with a value of \$1,433 were charged back to cash in June 1973, after we presented a list of outstanding checks to MWO officials.

RECORDS AND DOCUMENTS

Our review of files relating to real estate owned and mortgage loans showed that there is a need for improvement in the control of records and documents.

| <u>Account</u> | <u>Description of activity</u> | <u>Account balance at 12/31/72</u> |
|----------------|--------------------------------|------------------------------------|
| 1310 | Real Estate Contracts | \$13,117,597 |
| 1320 | Real Estate Owned | 20,866,105 |

Our examination of real estate contracts and real estate owned files disclosed instances where pertinent documents necessary to support the individual balances, such as the deed, title, insurance policy, or appraisal reports, were missing from the files. Appraisal reports relating to real estate contracts could not be found, and in the case of real estate owned, a total of 40 out of 47 files examined had one or more documents missing. In addition, our review of mortgage loans, Acct. 1010, disclosed that several appraisal reports and one complete loan file could not be located. MWO officials agreed that more control over the removal of records and documents from the files is needed. A form in each file showing the status of documents would be helpful.

LEDGER ACCOUNTS

After the consolidation of about 19 general ledgers in August 1972, and as a result of the system being installed, there was an increase in the number of different general ledger accounts. However, many of the new accounts have had little or no activity, thereby raising the question as to the need for all the accounts. Examples follow.

| <u>Account</u> | <u>Description of activity</u> | <u>Account balance at 12/31/72</u> |
|----------------|---|------------------------------------|
| 1015 | Participation Mortgage Loans | \$ 116,853 |
| 1016 | Participation Mortgages - Inter Office | 1,709,001 |
| 2475 | Accounts Payable - Participation Mortgages - Other | 58,837 CR. |
| 2476 | Accounts Payable - Inter-Office Participation Mortgages | 1,709,001 CR. |

During 1971 two asset accounts were maintained to record participation mortgages--Acct. 1016 -- Participation Mortgages - Other and Acct. 1017-- Participation Mortgages - Inter-Office. In 1972 Acct. 1017 was closed out, Acct. 1016 was redesignated, and Acct. 1015 established. Off-setting liability accounts existing in 1971 have never been redesignated.

| <u>Account</u> | <u>Description of activity (Contd.)</u> | |
|----------------|---|------------|
| | MWO officials said that Acct. 1017 was set up on a temporary basis to record certain errors relating to the sale of loans in Acct. 1100 - Serviced Mortgage Loans. Further, Acct. 1015 was established to distinguish between partially and fully participating loans which had previously been maintained in subsidiary ledgers for Acct 1016. | |
| 1920 | Deficiency Judgements | \$ 120 |
| 1921 | Rental Judgements | 1 |
| 2620 | Deferred Income from Judgements | 121 CR. |
| 3250 | Income from Deficiency Judgements and Direct Reductions | 21,114 CR. |
| 3251 | Income from Rental Judgements | 170 CR. |
| 4260 | Collection Fees - Deficiency Judgements | - |
| 4261 | Collection Fees - Rental Judgements | 57 |

During 1972, the recording of activity related to deficiency and rental judgements was changed, except for liabilities, from single accounts for assets, income, and expense to seven separate accounts.

MWO officials said that the decision to provide separate accounting for deficiency and rental judgements was made to assure that action was taken for settlement of judgement accounts. However, MWO is still in process of determining the number of judgements applicable to each account. In addition, MWO officials acknowledged that under the present method of billing used by attorneys servicing judgements, it is not possible to match income against the expenses involved.

| | | |
|------|--|--------|
| 4131 | Fraud and Bonding Legal Expense | 49,503 |
| 4132 | Civil Liability Legal Expense | 5,299 |
| 4133 | General Legal Expense - Loan Service Department | 6,981 |
| 4134 | General Legal Expense - Title Acquisition Department | 3,257 |
| 4135 | General Legal Expense - Administration | 33,189 |
| 4136 | General Legal Expense - Property Management Department | 808 |
| 4137 | General Legal Expense - Sales Department | 1,045 |
| 4371 | REO Legal Expense - Property Management | 1,687 |
| 4372 | REO Legal Expense - Sales Department | 1,754 |
| 4373 | REO Legal Expense - Loan Service Department | 1,075 |
| 4374 | REO Legal Expense - Title Acquisition Department | 15,142 |

Expenses recorded in Accts. 4131 through 4137 previously were recorded in Acct. 4133 which was then titled Legal

Expense. Charges to Accts. 4371 through 4374 were formerly charged to Acct. 4370, REO Legal Expense. We were told that the expansion of expense accounts was the result of the budget process and cost center approach to obtaining budget information. Another account, 4130 - Specific Legal and Loan Expense, was closed. MWO officials had no explanation as to how these expense classifications were to be used in the management of their activities.

RECONCILIATIONS

Differences between the accounts of the MWO and those of the Washington office which we could not reconcile are as follows.

| | <u>MWO</u> | <u>Washington office for MWO</u> |
|----------------------|-------------|--------------------------------------|
| Accounts Receivable | \$485,445 | \$547,833 |
| Miscellaneous Assets | 106,260 | 153,873 |
| Accounts Payable | 377,976 CR. | 277,976 CR. |