

# Office of Inspector General



Office of Audits and Evaluations  
Report No. AUD-12-010

---

**Controls Related to the FDIC's Contract with  
KeyCorp Real Estate Capital Markets, Inc.**

July 2012



## Why We Did The Audit

Within the FDIC, the Division of Resolutions and Receiverships (DRR) has primary responsibility for resolving failed FDIC-insured depository institutions, including the liquidation of assets in receivership. During 2010, DRR undertook an initiative to consolidate the servicing of loans and related assets in receivership with external "national" loan servicers, such as KeyCorp Real Estate Capital Markets, Inc. (KeyCorp). As of March 31, 2012, the FDIC had four national loan servicers that collectively serviced 3,182 assets with a net unpaid principal balance of about \$2.04 billion. KeyCorp was the largest of these servicers in terms of asset size, servicing \$1.23 billion (or 60 percent) of the \$2.04 billion.

In view of the significant role that KeyCorp plays in servicing receivership assets, the Office of Inspector General (OIG) conducted a performance audit of controls related to the FDIC's contract with KeyCorp. Our performance audit objective was to assess (1) the extent to which payments made by the FDIC for services provided by KeyCorp were adequately supported and in compliance with contract terms, (2) the reliability of selected data used to manage and market assets serviced by KeyCorp, and (3) the adequacy of certain controls over sensitive information handled by KeyCorp.

## Background

On July 26, 2010, the FDIC awarded a contract (referred to herein as "the Contract") to KeyCorp for the servicing of assets (primarily commercial loans) in receivership. Under the terms of the Contract, KeyCorp provides a full range of servicing activities, such as maintaining loan files, performing loan administration, loan default management, and collection and cash management services, and assisting, as requested, with asset sale initiatives. As compensation for its services, the FDIC pays KeyCorp various types of fees, including monthly servicing fees and transaction fees for loan conversion activities, loss mitigation efforts such as loan compromises and restructures, and foreclosures. The FDIC also reimburses KeyCorp for pass-through costs, such as taxes and insurance, and advances pursuant to loan commitments. As of March 31, 2012, payments to KeyCorp under the Contract totaled almost \$23 million.

KeyCorp maintains a significant amount of data that are used to support important business decisions regarding the management and marketing of assets. Accordingly, it is critical that the data be reliable (i.e., accurate, and complete). To help ensure the reliability of this data, DRR has taken various steps, such as incorporating data quality requirements into the Contract, periodically testing the accuracy of loan data maintained by KeyCorp, and initiating an internal "Loan Data Structure Project" in 2011 to help ensure the accuracy of receivership data captured and maintained by DRR and its contractors.

Key controls for protecting sensitive information handled by KeyCorp include background investigations, confidentiality agreements, risk-level designations for contracts and contractor personnel, subcontractor approvals, and contract security provisions. The FDIC's Division of Administration (DOA), through the Contracting Officer, works with DRR to ensure that these controls are implemented. Further, the FDIC established the *Outsourced Service Provider Assessment Methodology* to provide security oversight of outsourced service providers, such as KeyCorp. The methodology considers various security information to establish quantifiable risk ratings and, based on those ratings, defines procedures for verifying security measures and processes. Collectively, the security controls referenced above help to ensure that contractor and subcontractor personnel meet the FDIC's minimum standards of integrity and fitness and that sensitive information is safeguarded from unauthorized disclosure.

**Audit Results**

The preponderance of payments made by the FDIC to KeyCorp were adequately supported and were in compliance with the terms of the Contract for the charges that we analyzed. The payment discrepancies that we identified were not material in relation to the total charges that we reviewed and were addressed prior to the close of the audit. Notwithstanding these results, the relatively high error rate in our sample indicates that a review by DRR of KeyCorp's billing procedures is warranted. In addition, invoices supporting the charges that we analyzed had been reviewed and approved by DRR prior to payment as prescribed by FDIC policy. However, in light of the large volume of charges and associated documentation, a more risk-based approach for reviewing servicer invoices could promote efficiencies and consistency in DRR's review processes.

DRR has taken a number of steps to ensure the reliability of data used to manage and market assets serviced by KeyCorp. However, DRR can achieve greater assurance regarding the reliability of such data by establishing and implementing a more structured data quality program that includes such things as objective metrics to measure data reliability, enhanced policies and guidance, and improved contract provisions that address ongoing data reliability.

The FDIC conducted preliminary security checks and obtained signed confidentiality agreements for all of the KeyCorp contractor and subcontractor personnel that we reviewed. However, we identified instances in which background investigations had not been initiated as required by FDIC policy. In addition, the risk level designation for the Contract needed clarification. Further, KeyCorp did not obtain the FDIC's prior written approval before engaging a subcontractor to work on the Contract or include certain security-related provisions in its subcontracts as required by the Contract. Finally, the FDIC was working to apply its *Outsourced Service Provider Assessment Methodology* to assess security risks and controls at KeyCorp. Addressing the security control weaknesses identified during the audit will increase the FDIC's assurance that sensitive information is adequately protected and that contractor and subcontractor personnel satisfy the FDIC's minimum standards of integrity and fitness.

We plan to report \$12,057 in unsupported questioned costs pertaining to the payment discrepancies identified during the audit in our next *Semiannual Report to the Congress*. The amount ultimately disallowed by the FDIC may change based on management's final decision after evaluating the findings and recommendations in the audit report.

**Recommendations and Corporation Comments**

The report contains seven recommendations intended to improve controls related to the accuracy and review of KeyCorp's invoices, the reliability of receivership data, and the safeguarding of sensitive information. The Directors, DOA and DRR, provided a joint written response, dated June 19, 2012, to a draft of the report. In the response, the Directors concurred with all seven of the report's recommendations and described completed and planned corrective actions to address the recommendations. As described in the report, DRR and DOA officials clarified actions that will be taken to address two of the report's recommendations subsequent to our receipt of management's written response. Further, we provided relevant portions of the draft report to KeyCorp for its review and informal comment. In response, KeyCorp provided us with the status of completed and planned corrective actions to address the issues described in the report. We considered the information provided by KeyCorp in finalizing our report.

# Contents

---

	<b>Page</b>
<b>BACKGROUND</b>	2
<b>AUDIT RESULTS</b>	6
<b>Payments to KeyCorp</b>	6
<b>Controls Related to Data Reliability</b>	10
<b>Controls Related to Sensitive Information</b>	13
<b>CORPORATION COMMENTS AND OIG EVALUATION</b>	17
<b>Appendices</b>	
1. Objective, Scope, and Methodology	18
2. Monetary Benefits Terms and Results	22
3. Glossary of Terms	24
4. Acronyms	26
5. Corporation Comments	27
6. Summary of the Corporation's Corrective Actions	31
<b>Tables</b>	
1. Summary of Assets Serviced by KeyCorp as of March 31, 2012	3
2. Summary of Payment Discrepancies	7
3. Discrepancies in Asset Type and Collateral Type Data Elements	11



**DATE:** July 3, 2012

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

Arleas Upton Kea, Director  
Division of Administration

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

**SUBJECT:** *Controls Related to the FDIC's Contract with KeyCorp  
Real Estate Capital Markets, Inc.  
(Report No. AUD-2012-010)*

This report presents the results of our audit of controls related to the FDIC's contract with KeyCorp Real Estate Capital Markets, Inc. (KeyCorp).<sup>1</sup> KeyCorp provides nationwide servicing of assets (primarily commercial loans)<sup>2</sup> in receivership on behalf of the FDIC.

Our performance audit objective was to assess (1) the extent to which payments made by the FDIC for services provided by KeyCorp were adequately supported and in compliance with contract terms, (2) the reliability of selected data used to manage and market assets serviced by KeyCorp, and (3) the adequacy of certain controls over sensitive information handled by KeyCorp. To address our objective, we reviewed KeyCorp invoices and supporting documentation, evaluated data reliability controls, and assessed contract and oversight controls designed to protect sensitive information.

We conducted this performance audit 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.

Appendix 1 of this report includes additional details regarding our objective, scope, and methodology. Appendix 2 contains monetary benefit terms and results. Appendix 3 contains a glossary of key terms, and Appendix 4 contains a list of acronyms.

---

<sup>1</sup> KeyCorp is a business unit of KeyBank USA National Association, which is a wholly-owned subsidiary of Cleveland, Ohio-based KEYCORP, one of the nation's largest bank-based financial services companies. KeyCorp engages in the origination of agency loans and the servicing of commercial real estate loans for others. The company's loan servicing business is based in Overland Park, Kansas.

<sup>2</sup> Certain terms that are underlined when first used in this report are defined in Appendix 3, *Glossary of Terms*.

## **BACKGROUND**

Within the FDIC, the Division of Resolutions and Receiverships (DRR) has primary responsibility for resolving failed FDIC-insured depository institutions, including the liquidation of assets in receivership. During 2010, DRR undertook an initiative to consolidate the servicing of loans and related assets in receivership with external “national” loan servicers, such as KeyCorp. As of March 31, 2012, the FDIC had 4 external loan servicers that collectively serviced 3,182 assets with a net unpaid principal balance of about \$2.04 billion. KeyCorp was the largest of these servicers in terms of asset size, servicing 972 assets totaling \$1.23 billion (or 60 percent) of the \$2.04 billion.

### **The KeyCorp Contract**

On July 26, 2010, the FDIC awarded Receivership Basic Ordering Agreement contract RECVR-10-G-0171 (referred to herein as “the Contract”) to KeyCorp. Under the terms of the Contract, KeyCorp provides a full range of servicing activities for assets in receivership. The Contract has an initial term of 3 years, three separate 2-year option periods, and a 1-year option period, for a total potential period of performance of 10 years. The FDIC typically awards separate task orders under the Contract for individual receiverships. The task orders identify the specific assets to be serviced by KeyCorp. As of March 31, 2012, the FDIC had awarded 101 task orders resulting in almost \$23 million in payments to KeyCorp.

Key activities to be performed by KeyCorp under the Contract include:

- Maintaining appropriate loan files and performing loan administration, including loan payment processing, escrow maintenance, and advances under unfunded commitments or for collateral protection.
- Conducting loan default management, such as monitoring delinquencies and loss mitigation activities, including loan restructures, modifications, compromises, and foreclosures.
- Performing collection and cash management services and monthly bank account reconciliations.
- Assisting, as requested, with asset sales initiatives and performing services related to owned real estate assets, as needed.
- Providing weekly and monthly reports of asset balances and related transactions.
- Ensuring the quality and integrity of loan data transferred to KeyCorp.

- Ensuring that all contractor and subcontractor personnel with access to sensitive information are subject to background investigations appropriate to the risk level of the Contract.

As compensation for its services, the FDIC pays KeyCorp various types of fees, including a monthly servicing fee that is based on the amount of the unpaid principal balances of the assets being serviced. The Contract defines three different types of loan-related assets to be serviced—mortgage loans; non-mortgage loans; and judgments, deficiencies, and charge-offs (JDC). Each of these three asset types has its own fee rates. Fee rates for mortgage loans and non-mortgage loans are dependent on whether the loans are performing or non-performing. In addition to monthly servicing fees, the FDIC pays transaction fees for loan conversion activities, loss mitigation efforts such as loan compromises and restructures, and foreclosures. The FDIC also pays fees based on the number and types of reports that KeyCorp produces. Further, the FDIC reimburses KeyCorp for pass-through costs, such as taxes and insurance, and advances pursuant to loan commitments. Table 1 describes the types and amounts of assets serviced by KeyCorp as of March 31, 2012.

**Table 1: Summary of Assets Serviced by KeyCorp as of March 31, 2012**

Type of Asset	Asset Status		Total	Percent
	Performing <sup>(*)</sup>	Non-Performing		
<b>Commercial Non-Mortgage Loans</b>				
Unpaid Principal Balance (000s)	\$19,355	\$158,207	\$177,562	15%
Asset Count	25	123	148	15%
<b>Commercial Mortgage Loans</b>				
Unpaid Principal Balance (000s)	\$566,776	\$396,372	\$963,148	78%
Asset Count	517	272	789	81%
<b>JDCs</b>				
Unpaid Principal Balance (000s)	NA	\$90,437	\$90,437	7%
Asset Count	NA	35	35	4%
<b>Total Assets</b>				
Unpaid Principal Balance (000s)	\$586,131	\$645,016	\$1,231,147	100%
Asset Count	542	430	972	100%

Source: Office of Inspector General's (OIG) analysis of data in the KeyCorp *Detail Trial Balance Report* for the month ended March 31, 2012.

(\*) For the purposes of this table, "performing" refers to loans that are less than 91 days past due.

### **Contract Administration and Oversight Management**

The FDIC's Division of Administration (DOA) has primary responsibility for issuing policies and procedures that govern the Corporation's contracting program. DOA has issued the *Acquisition Policy Manual* (APM), which defines policies and procedures for procuring goods and services and assigning key roles and responsibilities in all phases of the procurement process. According to the APM, the Contracting Officer (CO) has overall responsibility for ensuring compliance with the terms of FDIC contracts and for protecting the FDIC's interests in its contractual relationships. The CO's duties include

the appointment of an FDIC employee to serve as a contract Oversight Manager (OM) to monitor and evaluate the contractor's performance. The CO may also appoint one or more Technical Monitors (TM) to assist the OM with contract oversight authorities, duties, and responsibilities.

The CO assigned to the Contract has designated an OM and multiple TMs. The responsibilities of the OM and TMs are defined in formal appointment memoranda issued by the CO. The OM's appointment memorandum states that the OM is responsible for such things as approving invoices and ensuring that appropriate background investigations are obtained for contractor and subcontractor personnel. TMs are responsible for receiving and reviewing required reports, participating in periodic contract compliance reviews, and assisting the OM in the evaluation of invoices. Separate TMs have been designated to support critical areas, such as credit, legal, and accounting.

An important aspect of the FDIC's oversight of KeyCorp is DRR's periodic reviews to assess the company's overall compliance with the operational and credit-related requirements of the Contract. At the time of our audit, DRR had completed three such reviews and made a number of recommendations to improve KeyCorp's operations. In addition, DRR's Internal Review staff issued a report in July 2011 on the division's oversight of external loan servicers. The report concluded that commercial loan servicers under contract with the FDIC, including KeyCorp, were being effectively managed by DRR.

### **Data Reliability**

KeyCorp maintains a significant amount of data pertaining to receivership assets that are used to support important business decisions. Accordingly, it is critical that the data be reliable (i.e., accurate and complete). The Government Accountability Office's (GAO) November 1999 publication entitled, *Standards for Internal Control in the Federal Government*, identifies a number of internal control activities that organizations can consider implementing to promote accurate and complete computer-processed data. Such internal control activities include, for example, data edit checks, verifications, and reconciliations. According to the publication, organizations should design and implement internal control activities based on related costs and benefits.

In 2011, DRR initiated the "Loan Data Structure Project" to help ensure the accuracy of receivership data captured and maintained by DRR and its contractors. The project involves reviewing the definitions and associated business rules for more than 1,100 data fields to ensure that they are adequately defined and consistently applied as data flows through the various DRR business lines. As part of this effort, DRR is working to identify potential duplication and non-essential data elements. Further, because DRR has placed increased reliance on external loan servicers in recent years to collect, manage, and report data pertaining to receivership assets, DRR is coordinating with its external loan servicers, such as KeyCorp, on the project.

## Information Security

Key controls for protecting sensitive information handled by KeyCorp include:

- **Background Investigations.** FDIC Circular 1610.2, *Personnel Security Policy and Procedures for FDIC Contractors*, describes the FDIC's processes for ensuring that contractors and their personnel meet the FDIC's minimum standards of integrity and fitness. Generally, these processes consist of conducting preliminary security checks of contractors and their personnel and ordering background investigations from the U.S. Office of Personnel Management (OPM) for contractor personnel with long-term access to FDIC facilities, systems, or sensitive information.<sup>3</sup>
- **Confidentiality Agreements.** The APM requires authorized contractor representatives and all key contractor personnel to sign confidentiality agreements prior to receiving or collecting sensitive information. The purpose of the agreements is to mitigate the risk of unauthorized disclosure of sensitive information.
- **Subcontractor Approvals.** The Contract states that KeyCorp must obtain the prior written approval of the CO before engaging subcontractors to perform services on behalf of the Corporation. Such approvals are required, in part, to ensure that subcontractors and their personnel meet the FDIC's minimum standards of integrity and fitness.
- **Contract Security Provisions.** The APM requires that certain security provisions be included in FDIC contracts and subcontracts to safeguard sensitive information and ensure that contractors, subcontractors, and their personnel meet the FDIC's minimum standards of integrity and fitness.
- **Security Oversight.** The FDIC established the *Outsourced Service Provider Assessment Methodology* to provide security oversight of outsourced service providers, such as KeyCorp. The methodology considers various security information to establish quantifiable risk ratings and, based on those ratings, defines procedures for verifying security measures and processes.

Our audit included an assessment of the above controls as they pertain to KeyCorp.

---

<sup>3</sup> Preliminary security checks consist of such things as fingerprint criminal records checks and reviews of personnel security questionnaires and credit reports. OPM background investigations consist (at a minimum) of a National Agency Check with Inquiries, which is a search of federal investigative databases maintained by the Federal Bureau of Investigation and other federal agencies, together with written inquiries of employers, educational institutions, law enforcement agencies, and references. The scope of OPM background investigations is based on the risk level associated with the duties of the individual.

## AUDIT RESULTS

The preponderance of payments made by the FDIC to KeyCorp were adequately supported and were in compliance with the terms of the Contract for the charges that we analyzed. The payment discrepancies that we identified were not material in relation to the total charges that we reviewed and were addressed prior to the close of the audit. Notwithstanding these results, the relatively high error rate in our sample indicates that a review by DRR of KeyCorp's billing procedures is warranted. In addition, invoices supporting the charges that we analyzed had been reviewed and approved by DRR prior to payment as prescribed by FDIC policy. However, in light of the large volume of charges and associated documentation, a more risk-based approach for reviewing servicer invoices could promote efficiencies and consistency in DRR's review processes.

DRR has taken a number of steps to ensure the reliability of data used to manage and market assets serviced by KeyCorp. However, DRR can achieve greater assurance regarding the reliability of such data by establishing and implementing a more structured data quality program that includes such things as objective metrics to measure data reliability, enhanced policies and guidance, and improved contract provisions that address ongoing data reliability.

The FDIC conducted preliminary security checks and obtained signed confidentiality agreements for all of the KeyCorp contractor and subcontractor personnel that we reviewed. However, we identified instances in which background investigations had not been initiated as required by FDIC policy. In addition, the risk level designation for the Contract needed clarification. Further, KeyCorp did not obtain the FDIC's prior written approval before engaging a subcontractor to work on the Contract or include certain security-related provisions in its subcontracts as required by the Contract. Finally, the FDIC was working to apply its *Outsourced Service Provider Assessment Methodology* to assess security risks and controls at KeyCorp. Addressing the security control weaknesses identified during the audit will increase the FDIC's assurance that sensitive information is adequately protected and that contractor and subcontractor personnel satisfy the FDIC's minimum standards of integrity and fitness.

### Payments to KeyCorp

We used both statistical and non-statistical sampling techniques<sup>4</sup> to analyze 44 invoices that had been approved for payment to KeyCorp during the period July 26, 2010 through September 30, 2011. Specifically, we determined whether:

- the charges on the invoices were allowable under the terms of the Contract;

---

<sup>4</sup> A non-statistical sample is judgmental and cannot be projected to the intended population by standard statistical methods. See Appendix 1 for a detailed description of the sampling methodology used during the audit.

- charges pertaining to a non-statistical sample of loans on the invoices were supported by underlying documentation and, for fee invoices, were consistent with the fee rates defined in the Contract; and
- DRR personnel had reviewed and approved the invoices prior to payment.

In addition, we conducted a limited review of two non-statistically selected loans on two additional invoices to determine whether KeyCorp had used the correct collateral type and unpaid principal balance amounts when computing monthly servicing fees.

Except as noted in Table 2, payments made to KeyCorp were adequately supported and in compliance with the terms of the Contract for the charges that we analyzed. The payment discrepancies that we identified were not material in relation to the total charges that we reviewed and were addressed prior to the close of the audit. Accordingly, we are not making recommendations to address these payment discrepancies. In addition, the invoices supporting servicing fees and pass-through costs had been reviewed and approved by the OM prior to payment as prescribed by the APM. A brief description of each discrepancy follows the table.

**Table 2: Summary of Payment Discrepancies**

Item	Description of Discrepancy	Invoice Number	Amount of (Under) Over Payment
1	Incorrect collateral type used to calculate the loan service fee.	345	(\$2,330.61)
2	Incorrect collateral type used to calculate the loan service fee.	361	(\$41.72)
3	Incorrect collateral type and unpaid principal balance amount used to calculate the loan service fee.	215	\$2,257.50
4	Incorrect unpaid principal balance amount used to calculate the loan service fee.	164	\$764.56
5	Duplicate payment of legal expenses.	327	\$11,407.32
<b>Net Overpayment by the FDIC</b>			\$12,057.05

Source: OIG's analysis of sampled KeyCorp invoices.

### Items 1 and 2

KeyCorp incorrectly billed two non-performing commercial loans as non-mortgage loans instead of mortgage loans. Because the non-performing servicing fee rate for non-mortgage loans is lower than for mortgage loans, the FDIC was undercharged by the amounts listed in Table 2. In researching the discrepancies, KeyCorp determined that these same assets were incorrectly billed on invoices outside of our sample. Specifically, the asset pertaining to Item 1 was billed at the lower rate from February 1, 2011 through November 30, 2011, resulting in a total underbilling of \$23,306.20. In addition, the asset pertaining to Item 2 was billed at the lower rate from March 31, 2011 through August 15, 2011, resulting in a total underbilling of \$189.12.

KeyCorp established *FDIC Collateral Review Process* procedures that require the company's account managers to (1) review loan documentation after it is uploaded into KeyCorp's loan system and (2) enter an appropriate collateral type code (e.g., commercial mortgage loan, commercial non-mortgage loan) into the loan system. The collateral type codes determine the fee rates used when computing monthly servicing fees for assets in receivership. For both Items 1 and 2, KeyCorp's account managers either misinterpreted or overlooked documentation indicating that the collateral type code was a commercial mortgage loan.

### **Items 3 and 4**

KeyCorp calculated monthly servicing fees for two assets based on incorrect unpaid principal balance amounts, resulting in overcharges to the FDIC. Specifically, KeyCorp foreclosed on two non-performing mortgage loans but did not reduce the unpaid principal balance amounts on the invoices to reflect the foreclosure sale price until the month after the foreclosure took place. Further, KeyCorp did not change the collateral type on the invoice for one of the assets to a JDC until the month following the foreclosure. Because servicing fee rates for mortgage loans are higher than for JDCs, the FDIC was overcharged.

KeyCorp established *FDIC Invoicing* procedures for preparing, reviewing, and approving service fee invoices before they are submitted to the FDIC. The procedures require KeyCorp's Investor Reporting group to coordinate with various departments within the company to obtain supporting documentation for fees billed. For our sampled assets, KeyCorp's account managers provided Investor Reporting with documentation indicating that the loans had been foreclosed, and Investor Reporting included the appropriate foreclosure fee on the monthly invoice. However, for one of the assets, KeyCorp's procedures did not ensure that Investor Reporting adjusted the collateral type of the asset on the sampled invoice from a mortgage to a JDC. In addition, KeyCorp's procedures did not ensure that Investor Reporting reduced the unpaid principal balance amount for either asset on the sampled invoices to reflect the foreclosure sales proceeds.

### **Item 5**

On March 31, 2011, nine loans were transferred to KeyCorp from another loan servicer. Under the terms of the transfer, the other servicer was responsible for paying expenses (including legal expenses) on the loans through March 31, 2011 and KeyCorp was responsible for paying expenses subsequent to that date. In May 2011, the KeyCorp OM authorized KeyCorp to reimburse a law firm for expenses totaling \$11,407 that had been incurred between January and March 2011 on the nine loans. The KeyCorp OM advised us that the other servicer had not paid the law firm on a timely basis and that it would be in the FDIC's interest to pay the expenses in order to maintain the continuity of the law firm's work. KeyCorp's OM indicated that he had advised the other servicer's OM that KeyCorp would pay the legal expenses. However, the other servicer also paid the legal expenses and was reimbursed by the FDIC for the same \$11,407. Prior to our audit, the law firm had not refunded the duplicate payment, nor had the FDIC requested a refund.

## **KeyCorp's Internal Billing Procedures**

Although the payment discrepancies that we identified were not material in relation to the total charges that we reviewed, the error rate in our sample indicates that a review by DRR of KeyCorp's internal procedures for preparing fee invoices is warranted. Specifically, KeyCorp used an incorrect collateral type to calculate the monthly servicing fee for 3 (or 7.7 percent) of the 39 loans that we tested and an incorrect unpaid principal balance amount for 2 (or 5.1 percent) of the 39 loans. In addition, these discrepancies were not detected by KeyCorp's internal control processes. A review of KeyCorp's internal billing procedures could identify opportunities to mitigate the risk that the types of discrepancies identified during the audit go undetected.

## **FDIC's Review of KeyCorp's Invoices**

The APM and the OM and TM Appointment Memoranda establish roles and responsibilities for the review, evaluation, and approval or rejection of contractor invoices. In addition, the TMs that we spoke with were reviewing invoices, providing feedback to the OM, and seeking opportunities to reduce costs and achieve efficiencies, such as by eliminating unnecessary reporting costs. However, the OM indicated that TMs could benefit from guidance that clarifies expectations regarding the review of invoices. Such guidance could, for example, describe:

- a more risk-based approach for reviewing servicer invoices that include large amounts of charges and supporting documentation. Given that it may not be practical or cost-beneficial to review every charge on an invoice, an approach that considers dollar amounts, trends, or anomalies that would warrant a closer review may be prudent.
- the amount and type of documentation that TMs should maintain to support their review of charges.
- when a specialist should be consulted in assessing the reasonableness of costs, such as consulting with the Legal Division regarding legal expenses.

The TMs that we spoke with generally relied on their experience and professional judgment when reviewing invoices. Guidance could promote a more consistent and efficient approach to reviewing invoices. The OM also acknowledged that improved guidance on reviewing invoices could help to mitigate risks associated with TM turnover and varying degrees of experience at the TM level.

## **Recommendations**

We recommend that the Director, DRR:

1. Review KeyCorp's internal billing procedures to determine whether they adequately mitigate the risk that the types of exceptions identified during our audit go undetected. Based on the results of the review, take appropriate steps to ensure that controls pertaining to the accuracy, timeliness, and support for invoices are adequate.
2. Evaluate whether guidance for a more risk-based approach to reviewing servicer invoices is warranted and feasible.

## **Controls Related to Data Reliability**

DRR has taken a number of steps to ensure the reliability of data used to manage and market assets serviced by KeyCorp. However, DRR can achieve greater assurance regarding the reliability of such data by establishing and implementing a more structured data quality program that includes such things as objective metrics to measure data reliability, enhanced policies and guidance, and improved contract provisions that address ongoing data reliability.

### **Contractual Requirements for Promoting Data Reliability**

DRR included various requirements in the Contract that address data reliability. Specifically, the Contract requires KeyCorp to develop an automated process for converting loans from prior servicer systems and to reconcile the conversions while adhering to standard industry requirements for data integrity. The Contract also requires KeyCorp to validate the prime interest rate index and other data relevant to the servicing of adjustable rate loans within 60 days of conversion and to report the results of the review to the FDIC. During our site visit to KeyCorp in December 2011, representatives of the company walked us through their processes for performing automated loan conversions and reconciliations and validating interest rates. With respect to ongoing (post conversion) data reliability, the Contract requires a Data Quality Report and independent evaluations of the company's operations by loan servicer rating agencies.<sup>5</sup> At the time of our audit, DRR had not requested a Data Quality Report from KeyCorp or defined the expected content of the report.

### **DRR Control Practices for Promoting Data Reliability**

As part of the data conversion process, DRR verifies that selected loan data, such as account number, account name, and principal balance, have been correctly entered into KeyCorp's

---

<sup>5</sup> The Contract requires KeyCorp to provide the FDIC with the results of an independent evaluation of the company's operations by one or more loan servicer rating agencies. The results of the most recent evaluations available, which included reviews of KeyCorp's loan setup procedures for ensuring data quality, were favorable.

loan system. DRR also conducts periodic compliance reviews of KeyCorp’s operational and credit activities, which include validation of selected loan data to original source documents. In addition, DRR validates the quality of selected loan data through the use of third-party due diligence contractors prior to loan sales initiatives.

**Data Discrepancies**

As discussed in the previous finding, we identified discrepancies in key data elements, such as unpaid principal balance amounts and collateral types, maintained in KeyCorp’s system of record that resulted in erroneous billings and payments. In addition, as described below, we noted discrepancies between the collateral type data element reflected in KeyCorp’s records and the asset type data element reflected in the FDIC Communication, Capability, Challenge, and Control system (4C).<sup>6</sup> Because the FDIC uses the asset type data element in calculating the estimated losses on receivership assets, errors in this data element could affect the accuracy of the FDIC’s loss estimates.<sup>7</sup>

We identified 25 assets for which KeyCorp had notified DRR that the asset type data element assigned by the FDIC appeared inconsistent with the collateral type data element in KeyCorp’s records. We identified these assets based on a review of the same sample of invoices described in the prior finding. In each case, KeyCorp had provided the FDIC with loan file documentation supporting the collateral type for the asset. As reflected in Table 3, the asset type data element in 4C had been changed for only 5 of the 25 assets as of December 31, 2011.

**Table 3: Discrepancies in Asset Type and Collateral Type Data Elements**

Asset Type as Reflected in 4C	Collateral Type as Reflected in KeyCorp’s Records	Number of Assets	Asset Types Changed in 4C
015 - Commercial	Mortgage	12	0
015 – Commercial	JDC	1	0
030 – Mortgage	JDC	1	0
031 – Construction Mortgage	JDC	11	5
	<b>Totals</b>	<b>25</b>	<b>5</b>

Source: OIG’s analysis of selected KeyCorp invoices and related asset data in 4C.

<sup>6</sup> DRR Circular 7210.2 identifies the FDIC’s 4C system as an integrated, end-to-end Web-based application that provides full functionality to support franchise marketing, asset marketing, and asset management.

<sup>7</sup> The GAO conducts annual audits of the financial statements of the FDIC’s Deposit Insurance Fund and Federal Savings and Loan Insurance Corporation Resolution Fund. Those audits include a review of the FDIC’s loss estimates.

DRR personnel that we spoke with were unable to explain why the asset type data elements for the 20 assets had not been changed. The personnel added that a formal process had not been established to (1) review discrepancies between the asset type and collateral type data elements or (2) assess the need to change the asset type data element when appropriate. At the close of our audit field work, DRR had begun to develop written guidance for reviewing discrepancies between the asset type and collateral type data elements.

### **Data Reliability Metrics and Controls**

FDIC Circular 1301.3, *Enterprise Data Management Program*, states that the FDIC's policy is to manage all data efficiently and effectively, from a corporate perspective, in part, by ensuring that data supporting business operations is reliable, accurate, current, useful, easily accessible, and available in a timely manner. GAO's November 1999 publication entitled, *Standards for Internal Control in the Federal Government*, identifies internal control activities that organizations can consider implementing to promote accurate and complete computer-processed data. According to the publication, organizations should design and implement internal control activities based on related costs and benefits. In this context, organizations may, based on an assessment of risk, determine that data are reliable even though they are not error free. DRR took such an approach when it established its prior Data Quality Program in September 2005 to ensure "highly reliable and accurate data" within its priority IT systems. Under the prior program, critical data elements within DRR's priority IT systems were considered reliable if they demonstrated an accuracy rate of 90 percent or better based on data quality testing. Adopting a similar approach with respect to KeyCorp could help DRR determine whether errors identified in KeyCorp's data are within acceptable ranges. It would also facilitate DRR's ongoing efforts to assess the adequacy of data reliability controls, both in the Contract and in DRR's oversight management activities.

DRR Circular 7210.2, *Use of 4C for Franchise Marketing, Asset Marketing and Asset Management Activities*, dated November 18, 2008, established a data quality improvement process for internally managed assets. However, the circular does not reflect DRR's current business model of relying on servicer systems, rather than the FDIC's 4C system, as the authoritative source of data used to manage and market receivership loans. Consequently, DRR personnel had not implemented the data quality improvement process in Circular 7210.2 for loans serviced by KeyCorp. During our audit period, DRR had begun to assess the use of the FDIC's 4C system in the current business environment and whether to modify or rescind Circular 7210.2, as appropriate.

Absent additional data reliability controls, the FDIC has reduced assurance that data used to manage and market receivership commercial loans is reliable. In addition, the FDIC may not be managing corporate data in the most efficient manner by taking full advantage of the various procedures performed by KeyCorp and DRR personnel to ensure data quality and integrity. In particular, we noted that prior to marketing certain receivership loans serviced by KeyCorp, DRR had contracted with third-party due diligence firms to validate the quality of data that may already have been validated by KeyCorp or DRR personnel. Given the significant amount of data and number of parties involved with receivership assets, including external loan servicers, it is important for the

FDIC to have an integrated approach for ensuring that receivership loan data used to facilitate asset management and marketing decisions are reliable.

## **Recommendation**

We recommend that DRR:

3. Establish and implement a more structured program for promoting the reliability of receivership data. Such a program should consider the data reliability issues described in this report, such as:
  - ensuring the accuracy of asset type data,
  - updating current policy and guidance to reflect DRR's use of contractor systems to support asset management and marketing,
  - developing objective metrics to measure data reliability, and
  - ensuring current and future contracts contain clearly defined provisions for ongoing data reliability.

## **Controls Related to Sensitive Information**

The FDIC conducted preliminary security checks and obtained signed confidentiality agreements for all of the KeyCorp contractor and subcontractor personnel that we reviewed. However, we identified instances in which OPM background investigations had not been initiated as required by FDIC policy. In addition, KeyCorp did not obtain the FDIC's prior written approval before engaging a subcontractor to work on the Contract or include certain security-related provisions in its subcontracts as required by the Contract. Finally, the FDIC was working to apply its *Outsourced Service Provider Assessment Methodology* to assess security risks and controls at KeyCorp.

### **Background Investigations and Confidentiality Agreements**

We selected a non-statistical sample of 12 KeyCorp contractor and subcontractor personnel to determine whether the FDIC had initiated an appropriate background investigation and obtained a signed confidentiality agreement. We found that the FDIC conducted preliminary security checks and obtained signed confidentiality agreements for all 12 personnel. However, the FDIC had not ordered an OPM background investigation for 3 of the 12 individuals who had access to sensitive receivership loan information, as required by FDIC policy.

FDIC Circular 1610.2, *Personnel Security Policy and Procedures for FDIC Contractors*, states that individuals designated as key personnel "who will not have direct operational duties under the task" will be subject to an integrity and fitness check prior to contract award. Consistent with Circular 1610.2, DOA's Security and Emergency Preparedness Section (SEPS) performed the required integrity and fitness checks and concluded that

the checks did not reveal any information that would preclude the individuals from obtaining a contract or contract work with the FDIC.

Circular 1610.2 also requires contractor and subcontractor personnel with access to sensitive FDIC information to provide the FDIC with a completed Standard Form (SF) 85P, *Questionnaire for Public Trust Positions*, and to have an OPM background investigation commensurate with the risk level of their position. A completed SF 85P is a prerequisite for ordering an OPM background investigation. None of the three individuals that we identified as exceptions had submitted a completed SF 85P because Circular 1610.2 does not require the form to be submitted as part of the pre-award integrity and fitness check and the OM did not ask these individuals to provide the form due to an oversight. The KeyCorp Project Manager advised us that KeyCorp was not aware that further investigation of these individuals was needed given the FDIC's preliminary approval prior to contract award. After we brought this matter to DRR's attention, the OM requested that KeyCorp direct the three individuals to complete SF 85Ps, and KeyCorp subsequently submitted the forms to the FDIC. Prior to those submissions, the lack of OPM background investigations for the three individuals reduced the FDIC's assurance that they satisfied the FDIC's standards for integrity and fitness.

### **Risk Level Designations**

OPM background investigations for 9 of the 12 contractor and subcontractor personnel that we reviewed were based on a risk level designation of "moderate." However, Section 7.5.09, *Risk Level Designation*, of the Contract states that the risk level for purposes of conducting background investigations is "high." We brought this discrepancy to the attention of DOA contracting and DRR oversight management officials. Subsequent to the close of our field work, the CO advised us that, after consulting with a DRR Information Technology Manager, the Contract would be modified to reduce the required level of background investigation to "moderate" based on the job duties and sensitivity of information to be handled for the Contract. The CO indicated that this new risk level should reduce the costs of the background investigations required by the Contract by as much as \$238,000. The CO also indicated that similar modifications would be implemented for the other external loan servicer contracts, potentially resulting in significant additional cost savings to the FDIC.<sup>8</sup>

### **Subcontractor Approvals**

KeyCorp did not obtain prior written approval from the CO before engaging one of its three subcontractors to work on the Contract. Provision 7.5.6-04, *Approved Subcontractors and Consent to Subcontract*, of the Contract requires prior written approval by the CO for all subcontractors that perform any of KeyCorp's responsibilities under the Contract. KeyCorp engaged the subcontractor in June 2011 to perform up to

---

<sup>8</sup> We did not evaluate the appropriateness of the FDIC's decision to lower the risk level rating for conducting background investigations under the Contract or under other external loan servicer contracts as part of the audit.

100 percent of the document scanning and indexing services under the Contract. In addition, KeyCorp personnel informed us that the subcontractor supported KeyCorp's mail room operations and performed other activities that involved access to potentially sensitive information, such as check and loan file documentation pertaining to FDIC receiverships. We identified the subcontractor as providing services under the Contract during our December 5, 2011 walkthrough of KeyCorp's offices in Overland Park, Kansas.

KeyCorp had not identified the subcontractor under the Contract or included the firm in its Subcontracting Plans<sup>9</sup> submitted to the FDIC because it considered the subcontractor to be a shared resource supporting multiple KeyCorp clients. As such, KeyCorp determined that the firm would not qualify as a subcontractor under the Contract. As a result, the FDIC did not have the opportunity to assess the subcontractor's qualifications, initiate background investigations of its employees, or obtain confidentiality agreements from the firm or its personnel. The CO advised us that KeyCorp was informed on December 5, 2011, that the subcontractor personnel should discontinue providing services under the Contract until such time as written approval is obtained from the FDIC. On December 7, 2011, KeyCorp submitted a revised Subcontracting Plan to the FDIC that identified the subcontractor under the Contract. The CO formally approved the subcontractor to provide services under the Contract on May 8, 2012.

### **Contract Security Provisions**

We reviewed two of the three KeyCorp subcontracts and found that KeyCorp did not include certain provisions related to protecting sensitive information and background investigations in the subcontracts as required by the Contract. KeyCorp's Project Manager was not aware of the requirement to include these provisions in the subcontracts. In addition, as previously noted, KeyCorp did not consider one firm to be a subcontractor for purposes of the Contract. Further, the FDIC's contract oversight activities did not include a review of KeyCorp's subcontracts to ensure that they included the required provisions. The lack of the referenced security provisions reduced the FDIC's assurance that subcontractor personnel would protect sensitive information consistent with the FDIC's policies and that subcontractor personnel satisfied the FDIC's minimum standards of fitness and integrity.

### **Security Oversight**

The FDIC uses its *Outsourced Service Provider Assessment Methodology* to provide security oversight of outsourced service providers, such as KeyCorp. The methodology employs a risk-based approach for addressing security risks and evaluating compliance with security-and privacy-related requirements. It also requires, among other things, that the FDIC complete various security- and privacy-related documents for outsourced service providers.<sup>10</sup> At the time of our audit, the FDIC was in the process of applying the

---

<sup>9</sup> Subcontracting Plans identify, among other things, the names and capabilities of subcontractors, the rationale for using subcontractors, and a description of the work to be performed by subcontractors.

<sup>10</sup> Such documents include an *Application Security Assessment*, *Privacy Threshold Analysis*, *Security Synopsis Statement*, and *Contract Clause Verification Checklist*.

*Outsourced Service Provider Assessment Methodology* to KeyCorp. Specifically, the FDIC was collecting security-and privacy-related information from KeyCorp and, in March 2012, conducted a site-visit of KeyCorp's data center.

In our 2011 information security evaluation report required by the Federal Information Security Management Act, we noted that the FDIC's Division of Information Technology was working with the Corporation's divisions and offices to identify all of the outsourced information services (and associated service providers) used by the Corporation.<sup>11</sup> Based on the large number of services and service providers identified through this effort, the report recommended that the FDIC complete the development and implementation of a formal strategy that defines a risk-based approach for applying the *Outsourced Service Provider Assessment Methodology* to the FDIC's inventory of outsourced information systems and services. DRR's application of the methodology is consistent with that strategy. When complete, the results of the methodology will provide the FDIC with a greater understanding of KeyCorp's controls and practices for protecting FDIC data and complying with the security-related provisions of the Contract.

As a result of our prior recommendation and the FDIC's ongoing corrective action, we are not making a recommendation to address security oversight. Recommendations associated with the other issues we identified related to the controls over sensitive information follow.

### **Recommendations**

We recommend that the Director, DRR:

4. Enhance existing controls for ensuring that contractor and subcontractor personnel provide the FDIC with completed SF 85Ps when appropriate.
5. Coordinate with DOA to modify the KeyCorp and other servicer contracts, as appropriate, to reflect a risk-based and cost-effective approach to completing background investigations for contractor and subcontractor personnel.

We recommend that the Director, DOA:

6. Enhance controls designed to ensure that (a) subcontractors are approved by FDIC contracting personnel prior to providing services under FDIC contracts and (b) subcontracts contain appropriate security provisions.
7. Coordinate with KeyCorp to ensure that all required clauses related to protecting sensitive FDIC information are included in KeyCorp's subcontracts.

---

<sup>11</sup> OIG report entitled, *Independent Evaluation of the FDIC's Information Security Program—2011* (AUD-12-002), dated October 31, 2011.

## **CORPORATION COMMENTS AND OIG EVALUATION**

The Directors, DOA and DRR, provided a joint written response, dated June 19, 2012, to a draft of this report. The response is presented in its entirety in Appendix 5. In the response, the Directors concurred with all seven of the report's recommendations and described completed and planned corrective actions to address the recommendations.

Subsequent to the receipt of management's response, DRR and DOA officials clarified actions that will be taken to address two of the report's recommendations. Specifically, a DRR official advised us that, in addition to the completed corrective actions described in management's response to Recommendation 1, DRR plans to review KeyCorp's internal billing procedures to determine whether they adequately mitigate the risk of the types of exceptions identified in this report and recommend enhancements as necessary. DRR plans to review KeyCorp's billing procedures by August 31, 2012. In addition, a DOA official advised us that, in addition to the planned corrective actions described in management's response to Recommendation 6, DOA is considering additional steps to promote awareness among OMs and TMs of the issues described in this report pertaining to subcontractor approvals and subcontract security provisions.

Before finalizing our report, we provided relevant portions of our draft report to KeyCorp for its review and informal comment. In a letter dated May 31, 2012, KeyCorp described the status of completed and planned corrective actions to address the issues described in the report. We considered the information provided by KeyCorp in finalizing our report.

A summary of the Corporation's corrective actions is presented in Appendix 6. The completed or planned actions are responsive to the recommendations, and the recommendations are resolved.

## Objective, Scope, and Methodology

---

### Objective

Our performance audit objective was to assess (1) the extent to which payments made by the FDIC for services provided by KeyCorp were adequately supported and in compliance with contract terms, (2) the reliability of selected data used to manage and market assets serviced by KeyCorp, and (3) the adequacy of certain controls over sensitive information handled by KeyCorp.

We conducted this performance audit from October 2011 to May 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

The scope of this audit included invoices approved for payment to KeyCorp from the award of the Contract on July 26, 2010 through September 30, 2011. To achieve the audit objectives, we performed the following procedures and techniques:

- Reviewed:
  - The Contract, including modifications and selected task orders.
  - Applicable FDIC and KeyCorp policies and procedures related to contract oversight, invoicing, data reliability, and protection of sensitive information.
  - Loan file documentation in KeyCorp's loan system, which we accessed through KeyCorp's secure Internet portal.
  - DRR compliance review reports completed for KeyCorp at the time of our audit.
  - Third-party review reports of KeyCorp's operations available at the time of our audit.
- Interviewed FDIC personnel with contract oversight or support responsibilities, including the CO, the OM, and various TMs.
- Interviewed KeyCorp officials and personnel responsible for contract performance.

## Objective, Scope, and Methodology

---

- Conducted a site visit and performed a walkthrough of the KeyCorp loan servicing facility during the week of December 5, 2011 in Overland Park, Kansas.
- Tested a sample of invoices<sup>12</sup> to determine whether DRR personnel reviewed and approved the invoices prior to payment and the invoices were for amounts allowed by the Contract. Our sample consisted of:
  - a statistically random sample of 40 invoices totaling \$1,055,578 that were taken from the population of 282 invoices less than \$300,000 dated between June 1, 2011 and September 30, 2011 that the FDIC had approved for payment to KeyCorp as of September 30, 2011. The 40 sampled invoices represented 25 percent of the \$4,215,291 in invoices less than \$300,000 approved for payment during that period.
  - all four invoices of \$300,000 or more that the FDIC approved for payment to KeyCorp during the period from Contract award on July 26, 2010 through September 30, 2011. These four invoices totaled \$1,543,219, or 13.6 percent, of the \$11.4 million approved for payment to KeyCorp through September 30, 2011.
- Tested a non-statistical sub-sample of 70 loans from the sampled invoices described above to assess the support for the amounts billed.
- Reviewed all significant month-end suspense balances to determine whether they had an impact on the service fees billed for the months of March through August 2011. We considered the balances to be significant if they were greater than or equal to \$500,000, or greater than or equal to \$100,000 and outstanding more than 30 days.
- Tested a non-statistical sample of 25 loans to assess consistency between the collateral type and asset type for the loans. The loans were in the FDIC's 4C system as of December 31, 2011. In each case, KeyCorp had identified an inconsistency between the FDIC assigned asset type for the loan and the collateral type assigned to the loan based on a review of collateral by KeyCorp.
- Tested a non-statistical sample of 12 contractor and subcontractor personnel out of a population of more than 100 personnel who potentially had access to

---

<sup>12</sup> We sampled from three types of invoices: (1) KeyCorp-prepared invoices for loan servicing fees; (2) KeyCorp-prepared invoices for pass-through costs that included, among other things, advances under unfunded commitments and advances for the protection of assets; and (3) FDIC-prepared invoices for other payments, such as forwarding to KeyCorp principal and interest amounts that had been sent to the FDIC by prior servicers.

## Objective, Scope, and Methodology

---

sensitive FDIC information, for evidence of background investigations and signed confidentiality agreements.

- Reviewed the narrative for a non-statistical sample of two of the three KeyCorp subcontracts to assess compliance with the provisions of the FDIC's contract with KeyCorp.

We used both statistical and non-statistical sampling techniques to support the findings, conclusions, and recommendations in this report. However, none of these sampling techniques can be used to project to the intended population by standard statistical methods. We performed the audit work at the FDIC's offices in Dallas, Texas, and KeyCorp's offices in Overland Park, Kansas.

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

Consistent with the stated audit objective, we did not assess the FDIC's or KeyCorp's overall internal control or management control structure. We relied on information in FDIC and KeyCorp information systems and reports and interviews of FDIC and KeyCorp personnel to understand and assess the specific internal controls relevant to our audit objective. These included controls over the preparation and review of invoices, controls to ensure the quality and integrity of data, and controls over sensitive information.

We obtained data from various FDIC and KeyCorp systems. Where appropriate, we corroborated data obtained from systems that were used to support our audit conclusions with information from various sources, including loan file documents and testimonial evidence. However, we determined that specific information system controls were not significant to the audit objective and, therefore, we did not evaluate 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. 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 was not part of the audit objective.

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

## Objective, Scope, and Methodology

---

### Prior Audit Coverage

We considered prior audit coverage of areas related to our audit objective, including the report entitled, *Independent Evaluation of the FDIC's Information Security Program—2011*, dated October 31, 2011. In that report, the OIG noted that the FDIC had developed a methodology for addressing security risks associated with contractor systems and assessing contractor compliance with security-and privacy-related contract requirements. However, the report concluded that work remained to implement the methodology and recommended that the FDIC complete the development and implementation of a formal strategy that defines a risk-based approach for applying the methodology.

## Monetary Benefits Terms and Results

---

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 recommendations 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.

As indicated on the next page, a total of \$12,057.05 in questioned costs were identified during this audit.

**Monetary Benefits Terms and Results**

---

**Monetary Benefits**

<b><u>Questioned Costs Description</u></b>	<b><u>Questioned Costs</u></b>
Incorrect Loan Service Fee Payments	\$649.73
Duplicate Payment of Pass-Through Cost	<u>\$11,407.32</u>
<b>Total Amount of Questioned Costs</b>	<b><u>\$12,057.05</u></b>

Source: OIG’s analysis of invoices as described in this report.

## Glossary of Terms

Term	Definition
<b>Background Investigation</b>	Includes various types of investigations conducted by OPM for the FDIC. All contractor personnel with long-term access to FDIC facilities, information technology systems, or sensitive information must undergo an OPM background investigation commensurate with the designated risk level associated with the duties of each position.
<b>Commercial Loan</b>	A credit initiated for business purposes that may be secured or unsecured. Security for commercial loans may include, among other things, accounts receivable, equipment, inventory, real estate properties, or a combination of assets.
<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>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>Fee Invoices</b>	Invoices that include servicing fees based on a loan's unpaid principal balance, collateral type, performance status; loss mitigation fees for activities such as compromises and restructures; foreclosure fees; and report preparation fees.
<b>Judgments, Deficiencies, and Charge-Offs</b>	A judgment is a court ruling entered for or against a party in litigation, usually for an unpaid amount due from a debtor. A deficiency is the remaining amount owed by a borrower when a foreclosure sale does not produce sufficient funds to pay a mortgage debt in full. A charge-off represents the uncollectable portion of a loan.
<b>Key Personnel</b>	Contractor personnel deemed essential and critical to the performance of the contract and who are contractually required to perform by the Key Personnel contract clause.
<b>Outsourced Service Provider Assessment Methodology</b>	A methodology developed by the FDIC that provides a risk-based process for addressing security risks associated with contractor systems and assessing contractor compliance with security-and privacy-related requirements.
<b>Pass-Through Costs</b>	Generally these costs include expenditures that satisfy unfunded loan commitments, such as construction advances, or that protect the FDIC's interest in an asset, such as legal fees, property taxes, and insurance.
<b>Risk Level</b>	An evaluative classification designation assigned to contracts or contract labor categories based on duties performed that have the potential for

**Glossary of Terms**

---

<b>Term</b>	<b>Definition</b>
	affecting the integrity, efficiency, and/or effectiveness of the Corporation's mission, and when misused, may diminish public confidence.
<b>Sensitive Information</b>	Any information, the loss, misuse, or unauthorized access to or modification of which, could adversely impact the interests of the FDIC in carrying out its programs or the privacy to which individuals are entitled.
<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.

---

**Acronyms**

---

4C	Communication, Capability, Challenge, and Control system
APM	Acquisition Policy Manual
CO	Contracting Officer
DOA	Division of Administration
DRR	Division of Resolutions and Receiverships
GAO	United States Government Accountability Office
JDC	Judgments, Deficiencies, and Charge-offs
OIG	Office of Inspector General
OM	Oversight Manager
OPM	Office of Personnel Management
SEPS	Security and Emergency Preparedness Section
SF 85P	Standard Form 85P
TM	Technical Monitor

## Corporation Comments



1601 Bryan Street, Dallas, TX 75201

Dallas Regional Office

**DATE:** June 19, 2012

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

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

Bret D. Edwards, Director /**Signed**/  
Division of Resolutions and Receiverships

**SUBJECT:** Management Response to the Draft OIG Audit Report Entitled,  
*Controls Related to the FDIC's Contract with KeyCorp Real Estate Capital Markets, Inc.* (Assignment No. 2011-087)

This is in response to the subject Draft Office of Inspector General (OIG) Audit Report, issued May 16, 2012. In its report, the OIG made two recommendations to the Division of Administration (DOA) and five recommendations to the Division of Resolutions and Receiverships (DRR).

**MANAGEMENT DECISION**

**Recommendation 1 (DRR):** Review KeyCorp's internal billing procedures to determine whether they adequately mitigate the risk that the types of exceptions identified during our audit go undetected. Based on the results of the review, take appropriate steps to ensure that controls pertaining to the accuracy, timeliness, and support for invoices are adequate.

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

**Corrective Action:** It should be noted that all billing discrepancies noted in this audit have been resolved. KeyCorp has reimbursed the corporation the sum of \$12,057.05 as of February 9, 2012. A more enhanced process has been implemented by KeyCorp to review the Asset Types (AT) against the loan documents at conversion from the receiverships. Any and all discrepancies identified are submitted by KeyCorp to the Oversight Manager (OM) and the Accounting Technical Monitor (TM) for approval to change. Also, KeyCorp has enhanced its quality control process to ensure the unpaid principal balances are correct where multiple fees may be applicable. To avoid duplicate billing issues between the loan servicer and the receivership or another loan servicer. KeyCorp has incorporated in the conversion calls the discussion on handling expenses pre-conversion and post-conversion. Additionally, KeyCorp is posting all loan balances immediately as it relates to foreclosures where multiple fees would be assessed

**Completion date:** April 30, 2012

## Corporation Comments

**Recommendation 2 (DRR):** Evaluate whether guidance for a more risk-based approach to reviewing servicer invoices is warranted and feasible.

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

**Corrective Action:** DRR will review current procedures for reviewing monthly invoices to determine if a more risk based approach is feasible. Currently the OM randomly selects various amounts in each category of loans to check for accuracy. A 100% review of incentives fees is performed by an Asset Management TM and the OM.

**Completion Date:** September 30, 2012

**Recommendation 3 (DRR):** Establish and implement a more structured program for promoting the reliability of receivership data. Such a program should consider the data reliability issues described in this report, such as:

- ensuring the accuracy of asset type data,
- updating current policy and guidance to reflect DRR's use of contractor systems to support asset management and marketing,
- developing objective metrics to measure data reliability, and
- ensuring current and future contracts contain clearly defined provisions for ongoing data reliability.

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

**Corrective Action:** DRR has implemented a formal process through the OM and accounting to update Asset Types when discrepancies are noted between the servicer's collateral/invoice type and the FDIC asset type. Additionally, exception reporting has been developed to allow DRR/Asset Management to monitor anomalies among the Asset Type, Asset Subtype and Collateral Code. A 4C data integrity program has been developed which includes identifying critical data elements and assigning ownership of asset types to ensure 4C data from the servicer is validated and is reliable.

A project team (Data Standardization Project) was established in the fall of 2011, with representation from Capital Markets, LLC Monitoring, Asset Marketing, Asset Management, and BIS, to review each of the existing loan data structures which contribute to current data integrity issues. This project team is near completion with a standardized Loan Data Structure which will support each post-closing business line managing or marketing loan assets. Additionally, the project team has recommended a modification to the servicers' Statement of Work to engage the external loan servicers to perform a documented data integrity process that validates the system data to the source documents. This will further enhance the asset management and asset marketing data both at conversion and on an interim basis during the year. This process enhancement will result in many benefits – most notable is that the servicer's system of record will be updated in real time as due diligence is completed ensuring that the Asset Marketing data structure file will match the asset management conversion file to the LLC's. Standardizing the

## Corporation Comments

Loan Data Structure will further improve DRR's ability to objectively audit the servicer's data integrity and due diligence effort. DRR will enhance its semi-annual audit program to conduct an expanded review of data fields deemed "critical" that will compare the servicer's system of record and the loan documents to ensure accurate reporting.

**Completion Date:** October 31, 2012

**Recommendation 4 (DRR):** Enhance existing controls for ensuring that contractor and subcontractor personnel provide the FDIC completed SF 85Ps when appropriate.

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

**Corrective Action:** The DRR Oversight Manager has implemented a monthly verification process of the personnel who have received clearance by FDIC Personnel Security Management against the contractor's list of personnel assigned to the FDIC contract. As personnel changes occur, the SF 85Ps will be required and obtained from the contractor prior to the start of the background investigation process. Additionally a procedural memorandum is being developed for the OMs to provide guidance in monitoring personnel changes to the loan servicing contracts.

**Completion Date:** September 30, 2012

**Recommendation 5 (DRR):** Coordinate with DOA to modify the KeyCorp and other servicer contracts, as appropriate, to reflect a risk-based and cost-effective approach to completing background investigations for contractor and subcontractor personnel.

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

**Corrective Action:** DRR, in conjunction with DOA/ASB, obtained approval to lower the Risk Level of all loan servicing contracts from a High Risk to a Moderate Risk resulting in a significant cost savings to the corporation without sacrificing control of sensitive information by the loan servicers. As of June 7, 2012, all loan servicing contracts have been modified to reflect a Moderate Risk Level. Copies of the relevant modifications have been provided under separate cover.

**Completion Date:** June 7, 2012

**Recommendation 6 (DOA):** Enhance controls designed to ensure that (a) subcontractors are approved by FDIC contracting personnel prior to providing services under FDIC contracts and (b) subcontracts contain appropriate security provisions.

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

**Corrective Action:** The policy and process for approving subcontractors after the initial award is clearly delineated in APM/PGI 5.603. Generally, after contract award, the oversight managers and technical monitors have the most contact with contractors through onsite visits, invoice

## Corporation Comments

approvals, etc. To stress the importance of the pre-approval requirement for subcontractors, DOA/ASB will revise the Oversight Manager and Technical Monitor Appointment Memoranda (FDIC Form 3700/22 and 3700/23) to include a reference to the requirement for subcontractor approval. The updated forms will be issued for new awards and when an oversight manager or technical monitor is changed. Regarding the flow down of the appropriate security provisions, DOA/ASB will revise PGI Section 6.406, Post-award Conference Agenda, to include an area related to flow down of contract provisions to subcontractors and specifically referencing appropriate security provisions.

**Completion Date:** September 25, 2012

**Recommendation 7 (DOA):** Coordinate with KeyCorp to ensure that all required clauses related to protecting sensitive FDIC information are included in KeyCorp subcontracts.

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

**Corrective Action:** DOA will request a copy of each KeyCorp subcontract to verify that all required clauses have been included.

**Completion Date:** August 15, 2012

## 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	<p>All billing discrepancies noted in this report have been resolved. In addition, KeyCorp enhanced its processes for ensuring the accuracy of asset types and unpaid principal balance amounts; took steps to mitigate the risk of duplicate payments; and began posting loan balances immediately for foreclosures.</p> <p>A DRR official also advised us that DRR will review KeyCorp's internal billing procedures to determine whether they adequately mitigate the risk of the types of exceptions identified in this report and recommend enhancements as necessary.</p>	August 31, 2012	\$12,057	Yes	Open
2	DRR will assess its current procedures for reviewing monthly invoices to determine whether a more risk-based approach is feasible.	September 30, 2012		Yes	Open
3	DRR has implemented a formal process to identify exceptions and update asset types, and developed a 4C data integrity program. Additionally, DRR is nearing completion of the standardized loan data structure project, which has recommended modifying the servicer's Statement of Work to require the loan servicers to validate system data. In addition, DRR will enhance its semi-annual audit program to conduct an expanded review of data fields deemed critical.	October 31, 2012		Yes	Open

## Summary of the Corporation's Corrective Actions

<b>4</b>	DRR implemented a monthly verification process in coordination with FDIC Personnel Security Management to ensure that SF 85Ps are obtained from contractor personnel when appropriate. In addition, a procedural memorandum will be developed for OMs to provide guidance in monitoring personnel changes on loan servicing contracts.	September 30, 2012		Yes	Open
<b>5</b>	DRR, in coordination with DOA, lowered the risk level ratings of all loan servicing contracts from high to moderate.	June 7, 2012		Yes	Closed
<b>6</b>	DOA will revise the OM and TM Appointment Memoranda to reference to the requirement for subcontractor approvals and revise the Post-award Conference Agenda to address subcontractor security provisions. A DOA official also advised us that DOA is considering additional steps to promote awareness among OMs and TMs of the issues pertaining to subcontractor approvals and subcontract security provisions.	September 25, 2012		Yes	Open
<b>7</b>	DOA will request a copy of each KeyCorp subcontract to verify that all required clauses have been included.	August 15, 2012		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.