
**AUDIT OF OCWEN FEDERAL BANK'S SERVICING OF RTC
MORTGAGE TRUST 1994-S2**

Audit Report No. 99-010
February 12, 1999



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**OFFICE OF AUDITS
OFFICE OF INSPECTOR GENERAL**

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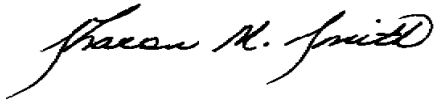
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DATE: February 12, 1999

TO: Douglas G. Stinchcum
Assistant Director, Asset Management
Division of Resolutions and Receiverships



FROM: Sharon M. Smith
Director, Field Audit Operations

SUBJECT: *Audit of Ocwen Federal Bank's Servicing of RTC Mortgage Trust 1994-S2* (Audit Report No. 99-010)

This report presents the results of an audit of Ocwen Federal Bank's¹ servicing of the Resolution Trust Corporation's (RTC) Mortgage Trust 1994-S2 (the Trust).² The Federal Deposit Insurance Corporation's (FDIC) Division of Resolutions and Receiverships (DRR) requested the Office of Inspector General (OIG) to conduct an audit of Ocwen's servicing of the Trust's transactions. DRR officials requested the audit because of concerns about Ocwen's management abilities, systems, internal communications, and failure to provide required reports.

BACKGROUND

The Trust was formed on August 10, 1994 to acquire and liquidate 88 assets. The RTC transferred the assets to the Trust under a deposit-trust agreement, and Wilmington Trust Company served as the trustee. The Trust was capitalized initially through the issuance of two classes of equity certificates with gross proceeds of \$29.6 million and the placement of a \$30.9 million bond secured by the assets of the Trust.

Unlike a typical contract where the FDIC, as successor to the RTC, engaged a third party to service assets owned by the Corporation, in this case the FDIC held a class B certificate. The FDIC's class B interest in this transaction represented 51 percent of the equity and conveyed the rights of a limited partner's interest in the Trust. The 1994-S-CA Investors Limited Partnership (the Partnership) held the class A certificate, which represented the remaining 49-percent share of the equity.

¹At the time that Ocwen Federal Bank became a party to the Trust, its name was Berkeley Federal Bank & Trust, West Palm Beach, Florida.

²As provided in the *RTC Completion Act of 1993*, the RTC went out of existence on December 31, 1995, and the Federal Deposit Insurance Corporation took over its functions on January 1, 1996.

Under the terms of the deposit-trust agreement, the day-to-day management decisions regarding trust operations were solely the responsibility of the class A certificateholder, which acted in the role of a general partner. This structure provided certain benefits to the FDIC, including insulation from lender liability claims against the Corporation. The Trust, rather than the FDIC, owned the assets. The agreements that created and governed the Trust prohibited the class B certificateholder from providing direction to the Trust, the servicer, or the class A certificateholder on day-to-day management decisions, operating policies and procedures, or liquidation decisions on trust assets.

Trust assets consisted primarily of nonperforming loans and owned real estate. The Partnership hired one of its partners, Ocwen, to service the Trust's assets. Ocwen and the Partnership, in turn, signed a subservicing agreement with Carbon Mesa Management and CCS Management. Under the subservicing agreement, Ocwen was responsible for accounting for the Trust's operations, and providing reports and certificates required by the various agreements, preparing all tax returns, maintaining the books and records, monitoring compliance, and managing 26 assets. Carbon Mesa Management was responsible for performing the asset management function³ on the remaining 62 assets, and CCS Management was responsible for providing analytical and marketing services, cash flow projections, and derived investment values. In addition, the subservicers could contract with independent contractors to perform any portion of their respective duties. Carbon Mesa Management contracted with at least 10 property managers to manage assets. The entities involved in owning, managing, and servicing the Trust's assets are presented in appendix I.

In July 1995, the RTC engaged AEW Capital Management, as successor to another third-party contractor, to oversee the RTC's limited partnership/class B certificateholder interest in the Trust. Generally, AEW was to monitor the actions of the servicer and ensure its compliance.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of our audit was to determine whether Ocwen accurately accounted for and reported trust receipts and claimed only allowable trust disbursements. To accomplish the objective, we interviewed personnel from (1) Ocwen in West Palm Beach, Florida; (2) Carbon Mesa Management in Santa Monica, California; (3) Carrick and Associates⁴ in Encino, California; and (4) AEW in Boston, Massachusetts. We also reviewed the deposit-trust, servicing, partnership, partnership-management, and subservicing agreements.

Table 1 shows the total receipts and disbursements that Ocwen recorded through October 31, 1997, and the amounts that we reviewed.

³The asset management function included preparing the individual asset business plan, carrying out the steps and procedures set for that plan, preparing updates to the plan, and preparing resolution memoranda.

⁴Carrick and Associates is one of the property managers subcontracted by Carbon Mesa Management.

Table 1: Trust Receipts and Disbursements Recorded and Amounts Reviewed

Receipts/Disbursements	Recorded	Reviewed
Initial setup deposits	\$ 3,517,592	\$ 3,517,592
Liquidation proceeds	56,951,905 ^a	15,010,355
Other receipts	12,966,103 ^b	1,472,947
Total Receipts	\$73,435,600	\$20,000,894
Estimated cash disbursements	\$ 8,005,347 ^c	\$ 2,330,406
Bond payments—principal	30,909,030	30,909,030
Bond payments—interest	2,728,372	2,728,372
Equity distributions	30,675,256	30,675,256
Servicing fees	1,054,415	1,054,415
Total Disbursements	\$73,372,420	\$67,697,479

^aTotal liquidation proceeds from Ocwen’s Loan Servicing and Management System (LSAMS) principal and interest payoff accounts.

^bTotal cash receipts from Ocwen’s Cash Flow Summary of \$69,918,008 minus the liquidation proceeds of \$56,951,905.

^cTotal cash payments from Ocwen’s Cash Flow Summary.

Source: OIG analysis of Ocwen’s monthly reports, LSAMS, and the Cash Flow Summary.

We judgmentally selected 14 assets with large and small loan balances and high volumes of receipt and disbursement activity. Ocwen had sold 13 of the 14 assets sampled at the time our audit ended. To determine whether Ocwen accurately accounted for real estate sales proceeds, we traced the proceeds from the closing statements to Ocwen’s Loan Servicing Accounting and Management System (LSAMS) for 12 of the 13 sold assets. Ocwen did not provide a closing statement for the remaining asset in our sample that had been sold. For other receipts (for example, rental receipts), we traced amounts recorded on Carbon Mesa Management’s receipt log to Ocwen’s LSAMS and monthly reports for 9 of the 14 sampled assets. The receipt log contained no postings for the remaining five assets. For the unsold asset, we also compared the recorded rental receipts to the tenant leases to determine whether Carbon Mesa Management received the correct amount. Tenant leases were not available for the sold assets.

To determine whether Ocwen claimed only allowable disbursements, we judgmentally selected disbursement transactions from Ocwen’s LSAMS transaction history inquiries and fee billing detail for the 14 sampled assets. We initially selected 94 large and small disbursements totaling \$640,821. However, because Ocwen did not provide either original invoices or checks for over 50 percent of the initial disbursement sample, we expanded our sample to include disbursement transactions for 44 assets. We selected the 30 additional assets from those with high volumes of disbursement activity and reviewed 106 disbursement transactions totaling \$1,689,585, which represented all disbursement transactions over \$4,999.

In total, we selected 200 disbursement transactions from August 1994 to September 1997 totaling \$2,330,406 for the 44 assets. We requested canceled checks, invoices, and other supporting documentation for the 200 disbursement transactions to determine whether the disbursements were adequately supported and allowable under the terms of the deposit-trust and servicing

agreements. We also selected for review 10 adjusting accounting entries that Ocwen made, of which 1 reduced trust receipts and the remaining 9 increased trust disbursements.

We did not evaluate Ocwen's system of internal controls. Instead, we relied on substantive testing to determine whether Ocwen accurately reported trust receipts and claimed only allowed trust disbursements. [material redacted] The OIG conducted the audit from November 1997 through November 1998 in accordance with generally accepted government auditing standards.

We met with Ocwen officials on August 12, 1998 to present the results of our audit. Subsequent to that meeting, on August 31, 1998, Ocwen provided written comments and additional documentation to address our findings. Ocwen's comments and our analysis of the additional documentation provided are incorporated in this report, as appropriate.

RESULTS OF AUDIT

Ocwen's monthly reports contained discrepancies and did not reconcile with its accounting system and source documents. For example, the beginning balance for a particular month often did not agree with the ending balance for the prior month. Moreover, we could not trace Ocwen's reports of receipts and disbursements to source documents for the initial 24 months of trust operations, and Ocwen did not comply with its reporting requirements. Further, we could not determine whether Ocwen accurately accounted for and reported receipts and disbursements of the Trust. We questioned \$957,108 in unallowable and unsupported trust transactions that included \$31,338 in unallowable legal and servicing fees, \$8,150 of unrecorded receipts, and \$917,620 of unsupported disbursements and accounting adjustments.

Based on our audit, the OIG recommended that the FDIC's Assistant Director, Asset Management, DRR, disallow \$957,108 in unsupported or unallowable trust transactions.

OCWEN'S MONTHLY REPORTS, ACCOUNTING SYSTEM, AND SOURCE DOCUMENTS DID NOT RECONCILE

Ocwen's monthly collection account activity reports—sent to the trustee, class A certificateholder, and FDIC—contained discrepancies and did not reconcile to Ocwen's accounting system or source documents. Specifically, the beginning balances on the monthly demand deposit account activity schedules often did not reconcile with ending balances from the preceding months' schedules. Moreover, we could not reconcile Ocwen's reports of receipts and disbursements for the initial 24 months to source documents. Accordingly, we could not determine whether Ocwen accurately accounted for and reported receipts and disbursements of the Trust.

Ocwen also provided monthly demand deposit account (DDA) collection activity schedules, which listed total daily deposits and withdrawals regardless of receipt or disbursement category, with inconsistent ending and beginning balances from one month to the next. For example, the ending balance on July 31, 1996 was \$4,364,359, while the opening balance on August 1, 1996 was \$4,402,918, an unexplained increase of \$38,559. Similarly, the ending balance on August 31, 1996 was \$1,610,785, while the opening balance on September 1, 1996 was \$1,581,720, an unexplained decrease of \$29,065.

In addition, Ocwen's monthly reports contained mostly summary receipt and disbursement information from the inception of the Trust through July 1996 that we could not reconcile to the source documents. For example, the monthly report for November 1994 included only a summary-level statement of cash receipts from operations, collections, deferred maintenance, and escrow accounts and a list of aggregate carrying values of the assets. It provided no details concerning the makeup and nature of individual transactions included in the summary-level and aggregate amounts. Because there was no audit trail to source documents, we could not determine whether Ocwen accurately reported specific collection transactions for the first 24 months. For example, we could not trace the sales proceeds for 5 of the 13 assets in our sample that sold prior to August 1996 to Ocwen's monthly reports. Similarly, we could not trace 47 of the 75 rental and other receipt transactions selected from Carbon Mesa Management's receipt log to Ocwen's monthly reports.

Because we questioned inaccuracies in its reports, Ocwen created a reconciliation of monthly reports with the asset-specific cash activity reported in LSAMS for each month from inception through September 30, 1997. That reconciliation included a calculation of estimated cash payments made through LSAMS and disclosed a difference of \$294,297 between the monthly reports and the asset-specific cash activity reported in LSAMS. Because this reconciliation disclosed a difference and additional work was needed to explain the discrepancy, we did not rely on the reconciliation.

Ocwen's counsel stated that criticizing Ocwen for failing to report auditable details was unfair because the servicing agreement did not require it to submit monthly reports containing auditable details. We disagree. Although the servicing agreement did not require reports containing auditable records, Ocwen is required, under the servicing agreement, to maintain source documents, records, and other reports that support various reports provided to the trustee, class A certificateholder, and the FDIC.

OCWEN DID NOT PROVIDE ADEQUATE SUPPORTING DOCUMENTATION FOR TRUST RECEIPTS, DISBURSEMENTS, AND ACCOUNTING ENTRIES

Ocwen did not provide adequate supporting documentation for trust receipts, disbursements, and accounting entries to the OIG for transactions that we reviewed. Specifically, Ocwen did not provide (1) a settlement statement for a sales transaction of \$8,858,433, (2) an explanation for posting \$38,184 more than the amount shown on a certain settlement statement, and (3) any record of a check for \$8,150 received from a property manager. Ocwen also did not provide

adequate supporting documentation for 42 of 200 sampled disbursement transactions totaling \$520,240 and for accounting entries totaling \$397,380.

Inadequate Support for Trust Receipts

Although Ocwen generally provided support for asset sales proceeds that we reviewed, it did not always maintain adequate support for rental and other receipts from trust assets. Ocwen provided support for the sales proceeds on all but 1 of the 13 sold assets in our sample. In addition, we could trace other receipts related to 9 of our 14 sampled assets from Carbon Mesa Management's records to LSAMS for all but one transaction. However, we generally could not verify whether property managers remitted correct amounts or Ocwen recorded all remittances.

For 11 of the 13 sampled assets that Ocwen disposed of during the audit period,⁵ Ocwen accurately recorded sales proceeds totaling \$13,390,480 based on the closing statements for each sale. For one of the sold assets in the sample, Ocwen recorded sales proceeds of \$1,619,874. Although the amount recorded exceeded the sales proceeds shown on the closing statement by \$38,184, Ocwen could not provide an explanation for the difference. For the remaining sold asset in the sample, Ocwen could not provide a closing statement for the sale. Ocwen recorded the asset sale as \$8,858,433; however, we could not verify the accuracy of that amount because the closing statement was not available.

In addition, Ocwen accurately recorded rental and other receipts posted to the property manager's receipt log for eight of the nine assets in our sample where Carbon Mesa Management remitted such receipts. Ocwen was unable to account for an \$8,150 check that Carbon Mesa Management received for a property, posted to its receipt log, and forwarded to Ocwen. The check represented primarily security deposits. The Partnership's servicing agreement with Ocwen required that Ocwen deposit principal and interest payments, insurance proceeds, asset sales proceeds, and any other receipts other than escrow receipts into its collection account. However, Ocwen did not provide documentation to show that it deposited the \$8,150 check. Accordingly, we questioned \$8,150 of unreported revenue.

Although we were able to determine that Ocwen, in general, recorded rental income and other receipts remitted by Carbon Mesa Management, we were unable to determine the accuracy of the amounts recorded by Carbon Mesa Management and Ocwen. Ocwen did not retain copies of leases for sold assets. Accordingly, we could not verify required lease amounts due under the leases except for the one unsold asset in our sample.

⁵One of the 14 sampled assets remained unsold at the time of our audit.

Inadequate Support for Trust Disbursements

Ocwen did not provide adequate supporting documentation for \$520,240 of the \$2,330,406 in disbursements sampled. Ocwen did not provide either originals or copies of supporting documentation for 42 of the 200 disbursement transactions sampled. Table 2 summarizes the disbursements that Ocwen did not adequately support.

Table 2: Trust Disbursements Not Adequately Supported

Available Support	Number	Amount
No check or invoice	13	\$203,450
No adjusting journal entry or debit memorandum	5	70,501
Original check only	9	70,553
Copy of check only	12	157,206
Copy of invoice only	3	18,530
Totals	42	\$520,240

Source: OIG analysis of Ocwen’s invoices, canceled checks, and other disbursements documentation.

For 18 of the disbursements totaling \$273,951, Ocwen did not provide originals or copies of canceled checks, invoices, adjusting journal entries, or debit memorandums. Ocwen responded that 5 of the 18 transactions were suspense disbursements and voided entries that did not involve cash disbursements from the Trust. However, Ocwen failed to provide adjusting journal entries, debit memorandums, or other source documents to substantiate the nature of those transactions. Instead, Ocwen supplied internally generated detailed transaction history summaries that did not verify Ocwen’s statements. For 21 transactions totaling \$227,759, Ocwen also provided originals or copies of canceled checks but did not provide either originals or copies of invoices. For those transactions, there was no assurance that the disbursements related to trust assets or amounts disbursed were correct. For three of the transactions totaling \$18,530, Ocwen provided copies of invoices but did not provide either originals or copies of canceled checks, adjusting journal entries, or debit memorandums. For those transactions, there was no assurance that Ocwen paid the invoices. Because of Ocwen’s failure to provide supporting documentation, we had no assurance that the disbursements were either allowable or accurate. Accordingly, we questioned the entire \$520,240 in unsupported disbursements.

Inadequate Support for Trust Accounting Entries

Ocwen did not provide adequate supporting documentation for accounting entries totaling \$397,380 that reduced trust receipts by \$8,817 and increased trust disbursements by \$388,563 in LSAMS.6 For the adjusting entry related to receipts, Ocwen posted \$224,626 in checks received from Carbon Mesa Management to the Trust’s collection account and subsequently made an adjusting entry that reduced those receipts by \$8,817. However, Ocwen did not provide any

⁶These adjusting accounting entries are separate from the 200-item disbursement sample. However, these entries are similar to the disbursements discussed earlier in that they have the same effect of increasing Trust disbursements and decreasing Trust income.

support for that adjustment. Accordingly, Ocwen understated trust receipts by \$8,817.

Ocwen also made nine accounting adjustments using transaction code FB-00 that increased the trust disbursements in LSAMS by \$605,570. Ocwen subsequently reversed six of the nine adjustments totaling \$217,007. However, Ocwen did not reverse the remaining three adjustments totaling \$388,563, which included a \$100,000 adjustment posted in April 1995, a \$248,563 adjustment posted in October 1996, and a \$40,000 adjustment posted in November 1996.

Ocwen's counsel stated that the FB-00 adjustments were noncash entries and were not accounted for as cash disbursements in the monthly reports to the Trust. However, Ocwen included the \$248,563 and \$40,000 amounts in the schedules attached to the October 1996 and November 1996 monthly collection account activity reports, respectively. In addition, Ocwen included the \$40,000 amount as a withdrawal on its November 1996 collection account activity report. Because the \$100,000 adjustment occurred in April 1995 during the initial 24-month period of trust operations when no detailed disbursement information was available, we could not determine whether Ocwen listed that amount in the monthly report for April 1995. Accordingly, at least two of the three adjustments were included in Ocwen's monthly collection account activity reports to the Trust, which contradicts the assertion by Ocwen's counsel that the FB-00 adjustments were noncash entries. Because Ocwen did not provide supporting documentation or reversing entries for the \$388,563 in fee bill adjustments, we questioned the entire amount as unsupported disbursements.

OCWEN MADE UNALLOWABLE DISBURSEMENTS FOR LEGAL AND ASSET-SERVICING FEES

Ocwen made unallowable disbursements for legal services and asset-servicing fees totaling \$31,338. For one of the disbursements in our sample, Ocwen obtained the authorizations of asset management and legal department officials to pay \$6,166 of a legal fee bill. However, Ocwen paid \$9,517 billed by the law firm—\$3,351 more than was approved. In addition, Ocwen miscalculated its own asset-servicing fees, which resulted in an overpayment of \$27,987. The servicing agreement authorized Ocwen to pay itself 1 percent of the principal balance of each trust asset that was less than \$1 million and .5 percent of the principal balance of each trust asset that was equal to or more than \$1 million. Ocwen's calculation of the servicing fees from the Trust's inception through October 31, 1997 showed that it overcharged the Trust by \$27,987. Accordingly, we questioned the \$31,338 of legal and servicing fees.

OCWEN DID NOT COMPLY WITH TRUST REPORTING REQUIREMENTS

Ocwen did not comply with the servicing and deposit-trust agreements' requirements to provide (1) an accountant's report and (2) partnership and servicer certificates to the trustee and the FDIC on an annual basis. Ocwen also did not provide any of the four required annual accountant's reports. Although Ocwen provided three of the four required annual sets of partnership and servicer certificates, they were incomplete and from 3 to 20 months late. Ocwen's failure to provide the annual accountant's reports as well as complete, timely annual certificates prevented the trustee and the FDIC from potentially identifying servicing weaknesses and taking timely

action to correct them during the early years of trust operations.

Annual Accountant's Reports Were Not Prepared

Ocwen did not provide the required annual accountant's reports⁷ for 1994 through 1997. Section 3.03 of the servicing agreement required Ocwen to annually hire an independent public accountant to perform certain agreed-upon procedures relating to Ocwen's compliance with servicing requirements and provide an annual report to the trustee and the FDIC. The servicing agreement required that the independent public accountant perform agreed-upon procedures related to Ocwen's servicing and management of the Trust's mortgage loans and real estate, respectively. The servicing agreement also required the accountant to comment on Ocwen's compliance with various requirements. Those requirements included initial contacts and inspections of mortgaged property, business plans, escrow collections, withdrawals, maintenance of insurance, deferred maintenance, environmental considerations, real estate titles, asset sales, and modifications to the agreement.

[material redacted]

⁷The annual accountant's report was also called the annual servicer compliance report.

[material redacted]

Partnership and Servicer Certificates Were Delinquent and Incomplete

Ocwen was late in providing the 1994, 1995, and 1997 partnership and servicer certificates to the trustee and the FDIC. In addition, the exception/default sheets for the 1994 and 1995 certificates were incomplete. The deposit-trust agreement required annual certificates for the Partnership and servicer by March 13 of the succeeding year attesting that the Partnership and servicer had fulfilled all material obligations in all material respects during the preceding calendar year. Ocwen's servicing agreement with the Partnership required Ocwen to prepare those annual certificates. The certificates were to provide the trustee and the FDIC some assurance that the Partnership and the servicer had fulfilled their material obligations under the agreements throughout the prior year. Table 3 summarizes Ocwen's late submissions of the certificates and provides information on the exception/default sheets that should have accompanied each certificate.

Table 3: Annual Partnership and Servicer Certificates

Year	Certificate	Months Late	Exception/Default Sheets
1994	Partnership	20	Blank
1994	Servicer	20	Missing
1995	Partnership	8	Blank
1995	Servicer	8	Missing
1996	Partnership	18 ^a	Certificates not provided
1996	Servicer	18 ^a	Certificates not provided
1997	Partnership	3	Disclosed three defaults ^b
1997	Servicer	3	Disclosed three exceptions ^b

^aThis equals the number of months late as of September 30, 1998.

^bThis includes an exception/default regarding Ocwen not providing the 1994 and 1995 annual accountant's reports.

Source: OIG analysis of Ocwen correspondence.

As table 3 shows, Ocwen submitted the certificates from 3 months to 20 months late. In addition, Ocwen had not provided the 1996 certificates as of September 30, 1998. For 1994 and 1995, Ocwen should have disclosed its failure to provide annual accountant's reports on the exception/default sheets. However, only the 1997 certificates disclosed that fact on the exception/default sheets.

[material redacted]

[material redacted]

CONCLUSIONS AND RECOMMENDATIONS

Because Ocwen's monthly collection account activity reports did not reconcile to other monthly reports or its accounting system and source documents, we could not determine whether Ocwen accurately reported trust receipts and disbursements to the trustee and the FDIC. In addition, Ocwen did not adequately support trust receipts, disbursements, and accounting adjustments or comply with reporting requirements. [material redacted] Accordingly, the OIG has no assurance regarding the accuracy or allowability of the remaining \$5.5 million in trust disbursements that we did not review.

Based on the results of our audit, we recommend that the FDIC's Assistant Director, Asset Management, DRR, take the following actions:

- (1) Disallow \$8,150 of unrecorded receipts that Ocwen received from Carbon Mesa Management (questioned cost of \$4,157 representing the FDIC's 51-percent share, all of which is unsupported).
- (2) Disallow \$499,549 of Ocwen's inadequately supported trust disbursements (questioned cost of \$254,770 representing the FDIC's 51-percent share, all of which is unsupported).

- (3) Disallow \$8,817 of Ocwen's unsupported adjustments to trust receipts (questioned cost of \$4,497 representing the FDIC's 51-percent share, all of which is unsupported).
- (4) Disallow \$388,563 of Ocwen's unsupported adjustments to the trust disbursements (questioned cost of \$198,167 representing the FDIC's 51-percent share, all of which is unsupported).
- (5) Disallow \$31,338 of Ocwen's trust disbursements for legal and servicing fees (questioned cost of \$15,982 representing the FDIC's 51-percent share).

CORPORATION COMMENTS AND OIG EVALUATION

On January 27, 1999, the Assistant Director, Asset Management, DRR, provided a written response to a draft of this report. The response agreed with the recommendations, with the exception of one transaction included in recommendation 2, and provided the requisites for a management decision on each of the five recommendations. The Assistant Director's response is presented as appendix II to this report.

A summary of the Assistant Director's response to draft recommendation 2 and our analysis follows. The response to recommendations 1, 3, 4, and 5 is not summarized because the actions planned or completed are identical to those recommended.

Disallow \$520,240 in inadequately supported disbursement transactions (questioned cost of \$265,322 representing the FDIC's 51-percent share) (recommendation 2): The Assistant Director generally agreed with the finding regarding Ocwen's inability to provide auditable documentation for its disbursement transactions. However, the Assistant Director disagreed with one transaction for \$20,691 that we included in the 42 questioned transactions totaling \$520,240. We concur with the Assistant Director's rationale for disagreeing. Accordingly, we have revised recommendation 2 to delete the \$20,691 transaction, which reduced the recommended disallowance to \$499,549 (questioned cost of \$254,770 representing the FDIC's 51-percent share, all of which is unsupported).

Appendix III presents management's proposed action on our recommendations and shows that there is a management decision for each recommendation in this report. Based on the audit work, the OIG will report questioned costs of \$477,573 (of which \$461,591 is unsupported) in its *Semiannual Report to the Congress*.

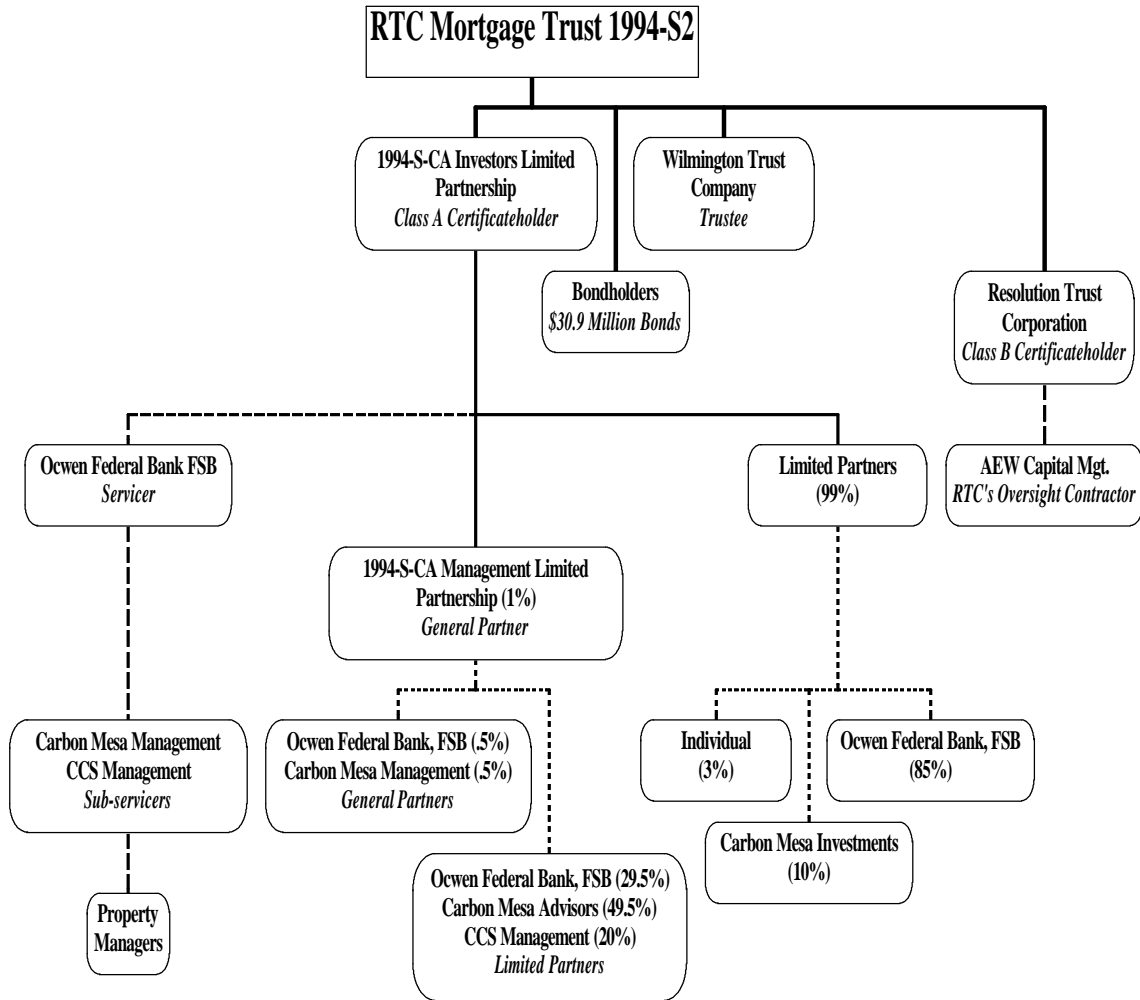
ENTITIES INVOLVED IN OWNING, MANAGING, AND SERVICING TRUST ASSETS

A number of entities, including several affiliates, were involved in owning, managing, and servicing the Trust. Wilmington Trust Company served as the trustee. Bondholders purchased \$30,909,030 in face value bonds secured by trust assets. Two classes of certificateholders retained \$29,636,996 of equity in those assets. 1994-S-CA Investors Limited Partnership held the class A equity certificate representing a 49-percent interest in trust equity, and the RTC held the class B equity certificate representing the remaining 51 percent of trust equity. The RTC hired AEW Capital Management to represent its interests in the Trust.

The 1994-S-CA Investors Limited Partnership had a general partner, 1994-S-CA Management Limited Partnership, and three limited partners—Ocwen, Carbon Mesa Investments, and an individual investor. The 1994-S-CA Management Limited Partnership had two general partners, Ocwen and Carbon Mesa Management, and three limited partners—Ocwen, Carbon Mesa Advisors, and CCS Management. Altogether, Ocwen had an 85-percent ownership interest in the 1994-S-CA Investors Limited Partnership.

Under the servicing agreement, Ocwen also serviced the Trust's loans and managed the Trust's real estate. 1994-S-CA Investors Limited Partnership and the Trust entered in a servicing agreement with Ocwen and, as allowed by the servicing agreement, Ocwen and 1994-S-CA Investors Limited Partnership signed subservicing agreements with Carbon Mesa Management and CCS Management. Figure 1 shows the interrelationships among the various businesses involved with the Trust as well as the percentage ownership in each preceding entity.

Figure 1: Major Entities Involved in RTC Mortgage Trust 1994-S2



Source: Ocwen organization chart and 1994-S-CA Investors Limited Partnership annual financial statements and partnership agreements.

CORPORATION COMMENTS

FDIC**Federal Deposit Insurance Corporation**

Washington D.C. 20429

Division of Resolutions and Receiverships

DATE: January 27, 1999

MEMORANDUM TO: Sharon M. Smith
Director, Field Operations
Office of the Inspector General

FROM: Douglas G. Stinchcum
Assistant Director
Division of Resolutions and Receiverships

SUBJECT: OLG Draft Report: Audit of Ocwen Federal Bank's Servicing of RTC
Mortgage Trust 1994-S2



On November 4, 1998 the Office of the Inspector General (OIG) issued its draft report on the results of an audit of **RTC Mortgage Trust 1994-S2**, in which the FDIC is the Class B Certificateholder. As noted in your memorandum forwarding the report, the OIG selected this Trust for review in response to DRR's request for an audit. FDIC-DRR requested this audit because of rising concern for numerous reporting discrepancies, management abilities and systems, and the repeated inability of the Servicer to provide timely or accurate reports.

The following are Management's responses to the specific recommendations of the audit report.

1. ***Disallow \$8,150 in unrecorded receipts that Ocwen received from Carbon Mesa Management (questioned costs of \$4,157 representing the FDIC's 51% interest).***

Management concurs with the finding. Ocwen has indicated in recent conversations that it is unable to locate any evidence that the check in question was negotiated by Ocwen or credited to the Trust's accounts.

2. ***Disallow \$520,240 in inadequately supported disbursement transactions (questioned costs of \$265,332 representing the FDIC's 51% interest)***

Management generally concurs with the OIG's finding regarding Ocwen's inability to provide auditable documentation for its disbursement transactions. One exception is noted at the end of

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this section. Ocwen could not adequately support both sides (invoice and check) by providing originals or copies of checks and invoices for many transactions. Without a proper invoice, OIG/DRR can have no assurance that the work was reasonable, proper or performed on Trust assets. Without a proper cancelled check or wire confirmation, OIG/DRR can have no assurance that a proper expense was actually paid.

For many of these disallowed/questioned costs, Ocwen was able to provide partial documentation, such as a cancelled check made out to a Tax Collector. But Ocwen failed to produce satisfactory evidence that the amounts paid were proper and that the Trust owned the subject properties at the time the taxes were paid. Similar findings were revealed in analyses of the Trust's vendor payments to law firms and property managers and receivers.

Management disagrees with the OIG's findings with regard to one of the entries. OIG selected as a transaction what was actually only a comment on an asset servicing screen. For asset #2263614 an entry dated 9/7/94 has the comment "...sent \$20,691.15 R/E tax bill to CMA for authorization..." The OIG interpreted this as an expense transaction when it was an asset manager's comment regarding a tax bill. DRR will therefore not disallow the \$20,691 (FDIC's 51% interest is \$10,552).

3. *Disallow \$8,817 in unsupported adjustments to Trust receipts (questioned costs of \$4,497 representing the FDIC's 51% interest),*

Management concurs with the OIG's related findings regarding the Servicer's failure to adequately document or support certain adjustments to the Trust's Loan Servicing and Accounting Management System (LSAMS) general ledger system. Ocwen has conceded that it does not have supporting documentation for these adjustments.

4. *Disallow \$388,563 in unsupported adjustments to Trust disbursements (questioned costs of \$198,167 representing the FDIC's 51% interest).*

Management concurs with the OIG's findings.

Ocwen cannot identify any offsetting credits for three "FB-00" adjustments, which had the effect of increasing Trust expenses by \$100,000 in April 1995, by \$248,563 in October 1996 and by \$40,000 in November 1996.

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5. Disallow \$31,338 in unallowable legal and servicing fee expenses (questioned costs of \$15,982 representing the FDIC's 51% interest).

Management concurs with the OIG's findings, which consists of two parts:

- (1) Ocwen's asset management and legal staffs approved partial payment of a \$9,517 legal services bill, authorizing payment of \$6,166 of the billed amount. Ocwen subsequently paid the full amount, which was \$3,351, more than the approved amount.
- (2) Ocwen appears to have miscalculated the asset servicing fees that it paid to itself under the terms of the Servicing Agreement. Ocwen's servicing fees were re-calculated by Ocwen in response to OIG's request for support for the fees paid to Ocwen since the inception of the Trust transaction. Ocwen's own recalculation from inception through October 31, 1997 indicates that Ocwen was paid \$27,987 more than should have been allowed under the definition found in the Servicing Agreement.

The OIG's audit report further identified problem areas for which no specific cost was identified, including Ocwen's failure to produce required reports in a timely and complete manner, and its failure to produce annual Partnership and Servicer Certifications as required under the terms of the Deposit Trust Agreement and the Servicing Agreement. Had these been prepared in a timely manner, management believes that many of the issues raised in the subject report could have been fully addressed before the situation became as difficult as it has become. However, as there are no assets remaining in the partnership, management need take no action on these issues.

Management anticipates resolving the disallowed cost issues raised in the OIG's audit report through the following procedure:

- (1) FDIC will issue, within ninety days, a demand letter to Ocwen that requests reimbursement for the FDIC's 51% interest in the disallowed costs.
- (2) FDIC will notify Wilmington Trust, the owner trustee for the 1994-S2 Trust, of the findings of the OIG report and management's action to recover the disallowed costs. The FDIC will request Wilmington Trust's cooperation in assuring that the Deposit Trust Agreement remains intact and does not terminate, and that no further distribution of its remaining assets be permitted until the disallowed cost issue is resolved.

cc: Gail Patelunas, DRR Nick Ravichandran, OIG Bruce Klink, AEW
Elliot Pinta, Legal Hank Abbot, DRR
Dean Eisenberg, DRR Jocelyn Spector, DRR

MANAGEMENT RESPONSES TO RECOMMENDATIONS

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

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

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

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

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

This table presents the management responses that have been made on recommendations in our report and the status of management decisions. The information for management decisions is based on management's written response to our report.

Rec. Number	Corrective Action: Taken or Planned / Status	Expected Completion Date	Documentation That Will Confirm Final Action	Monetary Benefits	Management Decision: Yes or No
1	The Assistant Director, Asset Management, DRR, agreed with the recommendation and stated that the Corporation would issue a demand letter to Ocwen for the FDIC's 51-percent share of the disallowed costs. He added that the Corporation would request the trustee to not make any further distribution of the Trust's remaining assets until the disallowed cost issue is resolved.	04/27/99	Demand letter and settlement agreement.	\$4,157 disallowed cost	Yes
2	The Assistant Director, Asset Management, DRR, agreed with the recommendation, as amended, and stated that the Corporation would issue a demand letter to Ocwen for the FDIC's 51-percent share of the disallowed costs. He added that the Corporation would request the trustee to not make any further distribution of the Trust's remaining assets until the disallowed cost issue is resolved.	04/27/99	Demand letter and settlement agreement.	\$254,770 disallowed cost	Yes

Rec. Number	Corrective Action: Taken or Planned / Status	Expected Completion Date	Documentation That Will Confirm Final Action	Monetary Benefits	Management Decision: Yes or No
3	The Assistant Director, Asset Management, DRR, agreed with the recommendation and stated that the Corporation would issue a demand letter to Ocwen for the FDIC's 51-percent share of the disallowed costs. He added that the Corporation would request the trustee to not make any further distribution of the Trust's remaining assets until the disallowed cost issue is resolved.	04/27/99	Demand letter and settlement agreement.	\$4,497 disallowed cost	Yes
4	The Assistant Director, Asset Management, DRR, agreed with the recommendation and stated that the Corporation would issue a demand letter to Ocwen for the FDIC's 51-percent share of the disallowed costs. He added that the Corporation would request the trustee to not make any further distribution of the Trust's remaining assets until the disallowed cost issue is resolved.	04/27/99	Demand letter and settlement agreement.	\$198,167 disallowed cost	Yes
5	The Assistant Director, Asset Management, DRR, agreed with the recommendation and stated that the Corporation would issue a demand letter to Ocwen for the FDIC's 51-percent share of the disallowed costs. He added that the Corporation would request the trustee to not make any further distribution of the Trust's remaining assets until the disallowed cost issue is resolved.	04/27/99	Demand letter and settlement agreement.	\$15,982 disallowed cost	Yes