



Gníomhaireacht Náisiúnta um Bhainistíocht Sócmhainní
National Asset Management Agency

6th December 2011

Mr. Michael Noonan T.D.,
Minister for Finance,
Department of Finance,
Upper Merrion Street,
Dublin 2

Dear Minister,

I am pleased to enclose a copy of the written report from Michael Geoghegan on his high level review of NAMA.

The Board welcomes this report as a substantial and important piece of work which confirms the progress made by NAMA to date and highlights some important challenges ahead. We have already begun to consider Mr. Geoghegan's recommendations and are charting an implementation plan which we would be glad to discuss with you at an early date.

We propose to publish the report on our website at a date to be agreed with you.

Yours sincerely,

Frank Daly
Chairman

-----Original Message-----

Sent: 02 December 2011 14:10

To: Frank Daly

Subject: High Level Review of NAMA

Dear Frank

You will shortly receive a finalised report arising out of my high level review of NAMA in accordance with and on the basis of my letter of engagement dated 26th September 2011.

I reiterate that the Board of NAMA is under no obligation to implement my recommendations and in light of the limited nature of this pro bono review, I encourage it to independently assess the recommendations and implement them only to the extent that it concludes, in its judgement, they are the best course of action for the Agency.

I confirm that a copy of the report can be provided to the Minister of Finance and if it is felt appropriate he may publish it.

As I am not in Ireland, I would appreciate receiving feedback from your Public Affairs Department on any public reaction to the review so that I remain informed and necessarily prepared.

I would like to take this opportunity to thank everyone at NAMA for the courtesy shown and assistance given as I carried out this review.

Best wishes

Yours sincerely,

Michael Geoghegan

NAMA Review :

Michael Geoghegan

Date: 2 December 2011

To: Frank Daly, Chairman, NAMA

As requested I am now providing a written summary of my final recommendations following my review of the Agency carried out within the following agreed terms of reference:

- a high level review of how NAMA is organised functionally,
- an assessment of the skill base at NAMA head of function level, and
- a high level evaluation of the delegation arrangements from the Board/Committees to Management.

I carried out the review during the period 26 September 2011 to 10 October 2011. The scope of the review has been limited to interviewing the Board Members, the senior Executives, certain other middle management, supporting Officers and both internal and external Auditors. Thirty six interviews were carried out. I would like to thank all those involved for their courtesy and assistance.

By its nature, this has been a limited exercise focussed on the organisational and structural elements of NAMA. My terms of reference do not go beyond that and I make no comment on any commercial or other approaches or decisions made by NAMA.

As agreed with NAMA I presented my recommendations orally and on a confidential basis to the Board and to the Minister for Finance on 10 October 2011.

Situation Analysis

Since NAMA was established in December 2009, an enormous amount of work has been done and a lot achieved in a very short time. In accordance with its mandate, by 30th September 2011, NAMA had valued, diligenced and purchased 11,500 loans from the participating Irish banks with a face value of €71 billion and a reported book value over €31 billion.

In this period, NAMA also began its task of realising assets, engaging actively with debtors on their business plans and managing its relationships with the participating Irish banks.

As this work was ongoing, NAMA as an organisation was assembled from the ground up. This is a notably complex task in an organisation of this scale as all of NAMA's personnel had to be identified, hired, integrated and organised while all of the agency's policies, systems and control mechanisms were simultaneously built.

In this initial stage of its development, it is unsurprising that the central theme in NAMA has been around control and accountability. This is heavily reflected in the NAMA Act, the constitution of the Board of NAMA and the use of executive resource in NAMA.

The Board of NAMA is comprised predominantly of directors with control rather than entrepreneurial backgrounds. It is a very active Board and its control focus, both directly and through Board Committees, consumes a very considerable amount of the available executive resource and focus in NAMA. This is manifested in the large number of internal meetings, long agendas and substantial numbers of attendees. The Chief Executive, who is respected by all for his ability to absorb a very intense workload, manages an extraordinary level of administration and is not liberated to focus on the more strategic or entrepreneurial aspects of the role.

This control focus is reinforced by the constant external scrutiny and comment, politically and in the media, much of which is negative.

In the formative stages of a key agency of NAMA's novelty, central public purpose and financial importance, none of these things are unexpected.

However, in my view it is now of fundamental importance that NAMA evolves further beyond this start-up phase and becomes the pro-active, externally focussed, entrepreneurial, confident business it needs to be (even when its actions may not immediately be popular politically or in the media). NAMA understands the need for this evolution and it's ability to make this transition effectively will define its ability to realise the kind of financial return for the Irish taxpayer which must be achieved from the assets it has purchased. A failure to complete this evolution is likely to cost the Irish taxpayer a number of billion euro and make the achievement of NAMA's key targets particularly challenging.

Of course efficient and effective controls need to be robustly maintained, but these should always operate in the background, not the foreground, and should not become an end in themselves. Their function should be to support, not inhibit, the business.

My recommendations therefore revolve around the steps which I believe should now be taken to refocus the Agency on the central theme of realising maximum value for the taxpayer from the assets it has purchased, just as a private company would. These include reinforcing the Executive, freeing the Chief Executive to focus on the value-added elements of the business and introducing greater entrepreneurial and property skill sets to the Board.

In summary, NAMA is pretty much at a point where I would have expected it to be at this juncture. There is no doubt there has been and there continues a huge personal commitment by all involved to ensure that NAMA is a success and my recommendations are made to assist that commitment.

Recommendations

The Board

The Board needs to satisfy itself that it has the right balance between oversight and management, the latter being the responsibility of the Executive.

The Board needs to be comprised of different skills and it needs to balance its current "control" features with those of entrepreneurial skills, ideally within the property industry but if this is not possible it should look within other industries. This is a matter which the Minister should consider in future appointments to the Board.

The Board should increase the number of Executive Directors to three¹ and the rest of the Executive team should not attend Board meetings unless they are presenting.

Board Committees

Membership of each Committee should be not more than five Directors with the Chairmanship rotated every two years.

No Executives should be in full attendance other than the Head of Audit². All other appropriate Executives should be on call to attend.

The agendas of each meeting need to be carefully planned out so that themes and subjects are not duplicated between the various Committees and over reviewed. The agenda of each Committee should be overviewed by the Board Secretary to prevent this unnecessary duplication.

The Board Chairman should appoint the Committee Chairpersons.

The Committee Chairpersons should be responsible for proposing the Committee membership to the Board Chairman for his approval.

The Executive

The Executive should meet monthly under the auspices of an Executive Committee. The Executive Committee should comprise all function Heads excluding the Head of Audit. There should be an agenda and proceedings should be minuted.

A summary report of the Executive Committee meetings should be presented to the Board as part of the CEO monthly reporting pack.

¹ Currently CEO is only Executive that is a ex officio Board member

² Recommended as a new organisational role, internal audit is currently outsourced to Deloitte

The agenda should be a mix between control and growth elements of the business. Heads' Goals and Measures should have a measure of his/her contribution at such Executive meetings. The intention is to create a rounded and collegiate team which will, over time, allow some Heads to switch into alternative roles within NAMA.

The Executive Committee must have the authority to act within broad enough decision making limits that allows the Executive to make decisions in a pro-active fashion. Thereby ensuring maximum value is achieved for NAMA assets in markets that will most likely be vulnerable to ongoing volatility and where assets will most likely be bought by international entities not requiring significant bank finance. Such entities expect an immediate and responsive level of engagement from the Executive which can only be achieved through a broad decision making capability being vested in the Executive on a day-to day basis.

The roles, skills and organisation of the current departments

- **Restructure of Portfolio Management, Credit and Risk, Lending and Legal Departments**

- 1) The primary relationship between the Debtor and NAMA should be managed by a (to be established) new Debt Restructuring unit. The staff for this department should come from parts of Portfolio Management and parts of Credit and Risk. Their primary initial focus would be on the 2013 debt reduction target but also keeping a watching eye on post 2013.

The industry skills to achieve this should be sought from the smaller specialised Portfolio Asset Management Team, who should act as day to day asset advisers to this Debt Restructuring unit.

- 2) The balance of property specialists in Portfolio Management should remain in Portfolio Asset Management, and they should be charged with improving as many existing assets as possible, thereby improving these assets for sale in 2014 and beyond. To achieve this, an appropriate Capex and borrowing limit of at least €500m will be required to be approved by the Board with the funding of this coming from asset sales already achieved.
- 3) Ideally, the 600 PI Managed connections should be brought in house and managed directly within the newly formed Debt Restructuring team. To give effect to this NAMA should recruit an additional 200 staff at a maximum cost of €25m. The additional staff cost of this should be capable of being offset by a lower administrative cost being paid to the PIs³. The management of these 600 cases represents a major risk to the recovery rate for NAMA as the PI's refocus their efforts towards their core business and will regard this business as potentially non-core. Failure to bring these assets onto NAMA's book in the next six months may increase the risk of NAMA failing to meet its bond repayment schedule

³ Currently 10 bps pa equivalent to €74m is paid to the PI's

- 4) A new and more senior role of Director of Risk should be appointed covering Operational Risk, Treasury Risk, Credit Risk and Legal Risk. The Director of Risk should be an Executive Director and his/her department should be staffed from those remaining in Credit and Risk after others have been transferred to the Debt Restructuring Team.
- 5) The mix of skills, capacity and deployment within the Legal Team need to be reviewed so that
 - (a) specific Solicitors are closer to their internal clients⁴ , and
 - (b) work which is currently being passed out to external firms is brought in house as much as possible.

New or Enhanced Skills

Chief Financial Officer

The need for the CEO to focus evenly on improving the revenue/recovery streams and controlling NAMA means that he needs to be able to re-balance his current workload by having a dedicated CFO⁵ full time in NAMA. The CFO should be an Executive Director charged with managing the following:

- A) Financial Operations and Financial Planning
- B) Business Services
- C) Tax

The CFO should deputise for the CEO in his absence, and should have sizeable operational limits so that little of anything administrative has to be approved by the CEO.

Head of Strategic Planning

A significant part of the CEO's role should be driving strategy forward through the strategic plan. On top of that an eight year exit strategy for NAMA needs to be developed and hence NAMA needs to start thinking now as to what size it will be and what experience it will have by the years 2017-2019, so that a possible trade sale could be achieved.

Apart from the Strategic Plan for NAMA itself, there needs to be clear Portfolio Strategies for dealing with different asset classes in different countries supported by a detailed schedule of asset sales per half year. These are at an advanced stage of development but need to be managed centrally within this Strategic Planning department

The substantial number of initiatives, directives and policies being created at present need to be set within a coherent Central Roadmap. This will pull together all the different

⁴ Debt Restructuring Team

⁵ The current CFO is part time and he has other responsibilities in the wider NTMA

departmental core initiatives, whilst providing a monthly rolling report as to where progress is being made and in turn identifying duplication and slippage.

Throughout the life of NAMA, it will be expected to develop and introduce new products and asset holding structures to assist with monetisation of the portfolio. These should be developed within Strategic Planning.

For all these reasons a Head of Strategic Planning needs to be appointed, reporting to the CEO.

Head of Audit

Although there are both internal and external audits, there are also others carrying out the same form of auditing, either in the name of Credit & Risk Quality Assurance team or Internal Controls reviews by Deloitte and NTMA's Head of Control.

As a startup organisation it is not unusual that controls should develop but NAMA has a myriad of control regimes which are utilising considerable resources. Over time consistent and efficient internal control policies need to be established with various core and supporting manuals. In the first instance this needs central direction through an Audit Function with an Audit Head who should also attend all the various Committees, thereby bringing some continuity of understanding. His/her reporting line should be direct to the Chairman of the Audit Committee with a dotted line to the Chairman of NAMA.

General Recommendations

- 1) Once a Debtor has been put into receivership in all or part, those elements in receivership should be administered by one specific insolvency team in the Debt Workout unit.
- 2) As NAMA is constantly being approached by workout specialists to take part of the portfolio to manage, and as certain people feel a third party management approach would achieve better results than those achieved by NAMA, consideration should be given to pass a small slice of the portfolio (€100-200m) to a third party and benchmark a similar size, same characteristic portfolio within NAMA and compare results.
- 3) Portfolio Stress Testing of the NAMA assets should be done taking account of the Financial Regulator's stress tests on the banks.
- 4) Impairment Provisioning for individual asset valuation changes should be accounted for at the annual Business Review or at a time when known deterioration has occurred, whichever is sooner. A half yearly report of changes in provisions should be submitted to the Board for approval.
- 5) A revised simpler credit grading system should be adopted and it is also recommended that a risk rating of 1 to 3 be used to assess each Debtor taking into consideration the co-operation of the Debtor and improvement or deterioration of the

value of the assets to the LAV. Both of these should sit alongside each other and trends should be monitored.

- 6) A Litigation Report should be prepared quarterly by the Head of Legal, showing the main actions being taken against the Agency, the likelihood of success or not and any likely financial cost to the Agency.
- 7) A semi annual report should be prepared showing amounts paid (over €500,000 in aggregate during the period) to third party professional providers. This should also include fees to loan brokers and estate agents.
- 8) All MIS should be held in one central Data Base and released only by CFO's Finance team. Data prepared not using the Data Base should not be allowed.
- 9) The Internal Auditors should be asked to audit the Data Base and the PMS system before the system goes live.
- 10) The new Head of Audit needs to look at the duplication occurring within the overall auditing function, and where possible agree with the internal and external auditors what audit work will be done by the Audit Department and what will be done externally, with the intention over time to reduce the costs of outside audit resources.
- 11) Whilst NTMA HR provides staff support, consideration should be given for a career development unit to be established within NAMA to manage future turnover and motivational issues. This could start with possibly a Skills Review for management below Executive level as part of this year's appraisal exercise. From this should also come the creation of a 3 and 5 year succession plan as personnel will leave NAMA and migrate back into the banking and property sectors as economic conditions improve.
- 12) A balanced scorecard approach to goal setting should be developed. All members of the Executive should have some form of financial goals within their overall goals.
- 13) With regard to remuneration, a robust long term plan modelled on private sector rather than public sector incentives is needed to ensure that remuneration of NAMA staff is tied into the long term performance of NAMA, to avoid any unnecessary turnover or loss of key staff. There is a major risk that the best staff will leave for the private sector and this could materially impair NAMA's abilities to secure the optimal financial return on its assets.

Delegation of Authorities

Credit Committee should only focus on assessing and approving (within limits to be defined) Business Plans, substantial subsequent amendments of the same, lending proposals, Capex, sales of loan portfolios (at below par) and sales of assets (below Business Plan agreed prices).

Generally, Boards do not approve Credit papers but note Credit Committee decisions. Normally a Credit Committee would see about 20% by value of facilities granted. In NAMA's case the Act expects a different approach, and it would be reasonable for the Board

to approve 10% of Credit by value after it has been recommended by the Credit Committee. It is unusual for a proposal to come for Board approval if first it has not been recommended by the Credit Committee.

Credit Committee should generally approve or recommend 30% by value of facilities/Business Reviews. The next 40% of Business Reviews by value should be approved by the CEO and the Head of Risk with the remaining 30% approved by the Head of Credit and Senior Managers in the Debt Restructuring Team.

If a credit rating for Business Reviews is adopted as recommended, then any credit downgrade of Business Reviews would need one level up approval from the level that originally approved it.

New money facilities would need to be added to the outstanding debt, and be approved on the basis of the new total.

The asset sale price range should be approved during the Business Review, and sales should be then executed within the range following sign off by the CEO.

Capex should be approved at the time of the Business Review, and only needs to be approved separately if the amount requested exceeds this Capex limit.

The CEO should have an expenditure limit, in keeping with him being able to approve 90% of the running costs of NAMA, above that it should be approved by the Board Chairman.

Conclusion

NAMA's publicly stated goals of repaying €7.5 billion of its debt by the end of 2013, €16.5 billion by the end of 2017 and €7.0 billion by end of 2019 will be what the Board and the Executive will be measured on by the shareholders-the people of Ireland.

While NAMA believes these goals are achievable it is questioned how much of the stock of assets will be used to meet the first goal and hence leave a shortfall of assets for the remaining goals. To avoid this it is imperative that NAMA does not just liquidate assets, it must also add value to assets so that this value can be realised in later years so as to meet the repayment schedule. It is the writer's opinion that NAMA must take this strategic long term view if it is to achieve its bond repayment schedule.

Because of the likely ongoing volatility of real estate prices in the countries where NAMA has exposure it is imperative that once a Strategic Plan to achieve the repayment schedule has been approved by the Board, the Executive is allowed to get on and implement its strategy in a resolute manner and within sensible response time parameters recognised by the market.

Failure to achieve any of these targets both by amount or time would no doubt create uncertainty and should possibly lead to the assets of NAMA being given to one or more third parties to manage.

The content of this pro bono report is based solely on the interviews described in the report, and on the Reviewer's own experience in managing similar situations. Review of supporting documentation or other verification has been very limited. Before being adopted for implementation each recommendation in this report should be independently assessed by the Board and the Executive and only implemented if they are satisfied, following more complete analysis, that what is suggested is in their judgement the best course of action. The Reviewer provides no warranties or other assurance in respect of any aspect of this report and the Reviewer emphasises that NAMA has no obligation to accept any or all of the said recommendations.