Federal Deposit Insurance Corporation
550 17th Street, NW, Washington, DC 20429 Deputy to the Chairman and Chief Financial Officer

November 22, 2010

TO: Board of Directors

FROM: Steven O. App
Deputy to the Chairman and
Chief Financial Officer

SUBJECT: Proposed 2011 Corporate Operating Budget

Proposal

This memorandum requests that the Board of Directors approve the proposed 2011 Corporate Operating Budget totaling $3,960,851,149, including $1,710,851,149 for ongoing operations and $2,250,000,000 for receivership funding.[1] The total proposed 2011 Corporate Operating Budget is $28,428,640 (0.7 percent) lower than the approved 2010 Corporate Operating Budget. The proposed ongoing operations component of the budget is $221,571,360 (14.9 percent) higher than the approved 2010 ongoing operations budget, while the proposed receivership funding component of the budget is $250,000,000 (10 percent) lower than the 2010 receivership funding budget.

Approval is also requested for a total authorized 2011 corporate staffing level of 9,252 (5,680 permanent, 3,572 non-permanent), up 223 positions from the currently-approved 2010 authorized staffing level of 9,029 (5,417 permanent, 3,612 non-permanent). This includes approval of individual division and office staffing authorizations, with limited flexibility for divisions and offices to temporarily exceed their permanent 2011 staffing authorizations.

Background

Structure of the Corporate Operating Budget

In 2003, the Board adopted the concept of an annual corporate operating budget with two components: ongoing operations and receivership funding. Funds approved by the Board for one component cannot be reprogrammed to pay for expenditures incurred for the other component. The segregation of annual operating expenditures into these two components was intended to facilitate more effective cost management by isolating the Corporation's more stable ongoing operational expenses from the variable annual expenses associated with bank closings and

[1]Certain factors that affect the Salaries and Compensation category of the proposed 2011 Corporate Operating Budget have not yet been finalized. For example, 2010 lump sum payments and bonuses for FDIC employees and the Corporation's share of employee health insurance costs have not yet been determined. When these factors are finally determined, they may require corresponding changes in estimated expenses for the Salaries and Compensation major expense category of the 2011 Corporate Operating Budget. As in prior years, the proposed 2011 Budget Resolution delegates authority to the Deputy to the Chairman and Chief Financial Officer to adjust the total Board-approved 2011 Corporate Operating Budget to account for such factors.

subsequent asset liquidation and litigation activities.

The receivership funding component provides funding for expenses incurred in connection with the failure (or near failure) of FDIC-insured institutions and the management of receiverships established in connection with those failures.[2] The establishment of the separate receivership funding component reflected a recognition of the fact that the number of failures and the expenses associated with those failures in any year are to a large extent outside of the control of the FDIC and that the actual expenses incurred for resolutions and receivership management activities may vary considerably from the estimates made during the annual planning and budget process.

From 2003 through 2007, the ongoing operations component was by far the larger of the two budget components, constituting over 90 percent of the total corporate operating budget each year due to the low level of resolutions and receivership management activity. The Corporation budgeted $75 million annually for receivership funding expenses during this period, but actual receivership funding expenses were considerably lower, ranging from $11 million to $40 million each year. However, as the condition of banking industry deteriorated and insured institution failures began to increase rapidly after 2007, the receivership funding component of the budget rose to $150 million in 2008, $1.3 billion in 2009, and $2.5 billion in 2010. By contrast, the ongoing operations component of the budget only rose from $1,032,489,659 to $1,489,279,789 during this period.

2011 Workload Analysis and Projections

During 2011, the Corporation will continue to focus largely on its core mission responsibilities, including the resolution of failed insured depository institutions and supervision of the historically high number of troubled and problem institutions that remain open. In addition, the Corporation will devote substantial resources in 2011 to the fulfillment of its new responsibilities under the *Dodd-Frank Wall Street Reform and Consumer Protection Act*. This will include the addition of the staff needed to review resolution plans submitted by large, systemically important financial companies and to be ready, if necessary, to resolve such companies.

As in prior years, the proposed 2011 budget is based primarily on an analysis of projected workload for each of the Corporation's three major business lines and its major program support functions. Corporate workload assumptions and guidance on planned initiatives were established at the outset of the annual strategic planning and budget formulation process, and divisions and offices determined their budget requirements in accordance with that guidance. As the proposed budget was finalized, these resource requirements were reassessed and refined in light of updated workload projections reflecting changing industry conditions. The Division of Insurance and Research (DIR) is expected to update these workload projections, in coordination

[2]Salary and benefits expenses for the permanent in-house staff associated with the Corporation's Receivership Management business line (primarily in the Division of Resolutions and Receiverships and the Legal Division) are funded from the ongoing operations component of the budget, because the maintenance of this in-house staff would be necessary, regardless of whether any failures actually occurred.

with the Division of Risk Management Supervision (RMS)[3] and the Division of Resolutions and Receiverships (DRR), at least semiannually during 2011. We will continue to monitor key workload indicators to ensure that authorized budget and staffing are adequate to address the projected workload. In addition, we plan to brief the Board on projected workload and resources in mid-2011, after DIR formally updates its workload forecast.

The Corporation's projected supervision and resolutions/receivership management workload are the primary determinants of the resource requirements reflected in the proposed 2011 budget. The most important driver of the Corporation's supervision workload is the number of institutions with composite CAMELS (risk management) ratings of 3, 4, and 5, because examinations of such institutions require substantially more time than examinations of 1- and 2-rated institutions. That number is expected to continue to rise for much of 2011, albeit at a slower pace than in 2009 and 2010. This will further increase the FDIC's 2011 examination and enforcement workload both for institutions supervised by the FDIC and those supervised by other Federal bank regulatory agencies. The proposed 2011 budget includes resources to conduct an estimated 2,588 risk management examinations and 1,791 compliance examinations of FDIC-supervised institutions, down slightly from 2010 due to failures and consolidation within the banking industry.

The primary drivers of the Corporation's resolutions and receivership management workload are the number of failures of FDIC-insured institutions and the amount of post-failure receivership work it is managing. The proposed budget reflects an expected decline in the number of insured financial institution failures in 2011, but continued growth in the volume of the number of post-failure receiverships being managed by the FDIC. There have been 149 failures of FDIC-insured depository institutions thus far in 2010, and the Corporation's inventory of assets in liquidation has fallen from approximately $41.4 billion (book value) at the beginning of 2010 to $33.8 billion (book value) on November 12. However, as of November 12, the Corporation was managing 333 active receiverships emanating from insured institution failures, up from 187 at the beginning of 2010. At the end of October, the Corporation was also overseeing 209 active loss share agreements with assets totaling approximately $191 billion (book value). A substantial volume of residual receivership management workload (asset management, asset sales, receivership claims, etc.) typically continues for several years beyond an institution's failure date.

2011 Budget Highlights

Overview of Proposed 2011 Budget by Component

The proposed 2011 Corporate Operating Budget totals $3,960,851,149, including $1,710,851,149 for ongoing operations and $2,250,000,000 for receivership funding (see

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[3] The Board approved in August 2010 the creation of separate divisions to manage the risk management (safety and soundness) and consumer protection supervision functions now administered by the Division of Supervision and Consumer Protection (DSC). A new Division of Depositor and Consumer Protection (DCP) will assume responsibility for consumer protection supervision functions in early 2011. DSC will retain responsibility for risk management supervision functions and will be re-named the Division of Risk Management Supervision at that time.

Attachment 1). This represents an increase of $221,571,360 (14.9 percent) in the ongoing operations budget component, offset by a $250,000,000 (10 percent) decrease in the receivership funding budget component.

The most significant factors contributing to the proposed increase in the ongoing operations component of the budget are further staffing increases for the Corporation's risk management and consumer protection supervisory programs in 2011; the implementation of a larger permanent staffing platform in DRR to ensure the Corporation's future readiness to resolve failed financial institutions; and the addition of a large number of new positions to fulfill the Corporation's new responsibilities under the Dodd-Frank Act. In addition to the permanent staffing increases in DRR, significant additional staffing is proposed in the Division of Risk Management Supervision (RMS), the Division of Depositor and Consumer Protection (DCP), the Legal Division, and the new Office of Complex Financial Institutions (CFI). These staffing increases will result in higher spending for salaries and benefits, travel, office space, equipment, and other expenses.

As we approach 2011, there continues to be a great deal of uncertainty regarding conditions within the banking industry and the Corporation's core supervisory workload. In addition, there are a number of open issues related to the resources that will be required to ensure that the FDIC effectively addresses the concerns reflected in the Dodd-Frank Act. For example, no final determination has yet been made regarding the resources that will be required in conjunction with the transfer of supervisory responsibilities for state-chartered thrift institutions to the FDIC from the Office of Thrift Supervision; the statutorily-mandated establishment of a new Office of Minority and Women Inclusion within the FDIC; or the possible creation of a new Chief Risk Officer function within the Corporation. Accordingly, the proposed 2011 ongoing operations budget includes an unassigned contingency reserve of $25,000,000 (approximately 1.5 percent of the proposed ongoing operations budget) to be administered by the Chief Financial Officer (CFO) to meet unbudgeted resource requirements that arise during the year.[4]

The most significant factor contributing to the proposed decrease in the receivership funding component of the proposed budget is the expected decline in financial institution failures in 2011, partially offset by increased receivership management workload. This workload will require fewer temporary staffing and contractor resources in DRR. This is consistent with the Corporation's established business model for resolutions and receivership management, which relies primarily on contractors and staff on time-limited appointments to handle temporary upticks in workload. The proposed budget for contractor support is $1,376,364,871, down $238,965,812 from 2010, and constitutes 61.2 percent of the proposed 2011 receivership funding budget. The proposed 2011 receivership funding budget also includes lower funding for travel, leased space, and equipment to support FDIC employees and contractors. To ensure that we have the flexibility to respond quickly to unexpected changes in workload, it also includes an unassigned contingency reserve of $16,703,153 (0.7 percent of the proposed receivership funding budget), to be administered by the CFO to meet unbudgeted resource requirements that arise during the year. Unassigned contingency funds totaling $175,826,625 were included in the

[4]The CFO will continue to report to the Board quarterly in 2011 on the reallocation of resources within the Corporate Operating Budget, including the use of funds from this contingency reserve.

2010 receivership funding budget approved by the Board in December 2010.

The proposed receivership funding budget is presented with a reminder that the FDIC cannot control the variable workload associated with this component of the annual corporate operating budget. The Corporation is not able to project with certainty the specific number and type of failures that will occur in 2011 or the actual expenses that will be incurred in connection with those failures. The proposed 2011 receivership funding budget should not, therefore, be regarded as a highly reliable estimate of 2011 expenses for this budget component. Based upon what is known today, we believe that the proposed receivership funding budget will be sufficient to cover 2011 resolutions and receivership management expenses, but we will return to the Board to seek additional funding if it is determined during the year that additional budget authority is needed.

Overview of Proposed 2011 Budget by Major Expense Category

Attachment 1 itemizes the proposed 2011 Corporate Operating Budget by major expense category. As in prior years, personnel-related expenses and contractor services constitute the largest expense categories in the proposed budget:

- The proposed 2011 Salaries and Compensation budget is $1,435,822,346, which is $158,201,087 (about 12.4 percent) higher than the 2010 Salaries and Compensation budget. This is attributable largely to the continued increase in proposed staffing authorizations in 2011 and to the fact that the Corporation will incur full-year salary and benefits expenses for the more than 1,900 new employees hired during 2010. The Salaries and Compensation expense category represents 64.2 percent of the proposed 2011 ongoing operations budget, 15.0 percent of the proposed 2011 receivership funding budget, and 36.3 percent of the overall proposed 2011 Corporate Operating Budget.

- The proposed 2011 Outside Services-Personnel budget (for contractor-provided services) is about $1,666,332,420, which is about $189,220,632 (10.2 percent) lower than the 2010 budget. This decrease reflects primarily an expected reduction in insured institution failures in 2011 and a resulting decrease in the contractor support required to close failed institutions. The Outside Services-Personnel expense category represents about 16.9 percent of the proposed 2011 ongoing operations budget, 61.2 percent of the proposed 2011 receivership funding budget, and 42.1 percent of the overall proposed 2010 Corporate Operating Budget.

The remainder of the proposed 2011 Corporate Operating Budget consists of Travel expenses ($151,576,363), up $3,555,837 (2.4 percent) from 2010, due largely to increased risk management and consumer protection staffing levels; Buildings and Leased Space expenses ($333,793,874), up $2,727,409 (0.8 percent) from 2010, to address increased office space requirements; Equipment expenses ($116,760,615), down $12,525,737 (9.7 percent) from 2010, as a result of the decreased number of FDIC employees and contractors planned for resolutions and receivership management activities; Outside Services-Other expenses ($47,991,727), down $641,380 (1.3 percent) from 2010 due to decreased receivership activity; and Other Expenses

($208,573,804), up $9,474,776 (4.8 percent) from 2010, primarily to cover higher administrative, training, and other expenses related to the projected continuing increase in the number of FDIC employees and receiverships.

Overview of Proposed Increases in Authorized 2011 Staffing

The proposed 2011 Corporate Operating Budget includes a total authorized staffing level of 9,252 positions (5,680 permanent, 3,572 non-permanent). This represents a net increase of 599 positions (448 permanent) over the authorized staffing level initially approved by the Board for 2010 and a net increase of 223 positions (263 permanent) over the current 2010 authorized staffing level.

If approved, the largest staffing increases will occur in the supervision program, with net increases for the combined RMS and DCP of 331 positions (94 permanent) over its initial 2010 staffing authorization of 3,780 positions and 314 positions (78 permanent) over its current staffing authorization of 3,797 positions. The largest permanent staffing increase is proposed for the new Office of Complex Financial Institutions (CFI), which has a proposed authorized staffing level of 156 positions (all permanent) in 2011. CFI had no staffing authorization at the beginning of 2010. In addition, the proposed 2011 staffing authorization includes a major increase in authorized permanent staffing for the resolutions and receivership management program. Although DRR's total authorized 2011 staffing will decrease by a net of 133 positions, its proposed permanent 2011 staffing authorization will increase by 118 positions.

Supervision

As noted above, the proposed 2011 Corporate Operating Budget provides for substantial additional increases in authorized staffing to address the Corporation's supervisory responsibilities beyond the increases that were approved for 2009 and 2010. These proposed increases largely reflect the following:

- An additional 201 risk management field examination positions (all non-permanent), bringing total field examination staffing to 2,698 (1,874 permanent, 824 non-permanent) to address the continuing increase in the number of insured institutions with composite CAMELS rating of 3, 4, and 5.[5]
- These additional risk management field examination positions would be supported by an additional 20 supervisory examiner positions (all non-permanent) and 7 regional office case manager positions (all non-permanent).
- An additional 24 positions (all permanent) to support DSC's residual large bank functions and its new responsibilities under the Dodd-Frank Act, including seven positions to staff a new section that will be responsible for reviewing resolution plans submitted by systemically important banks and bank holding companies with $50 to $100 billion in assets.
- An additional 29 positions (all permanent) to support the establishment of the new DCP.

[5] The 2,698 positions are comprised of 2,215 risk management examination positions (1,447 permanent, 768 non-permanent) and 483 compliance examination positions (427 permanent, 56 non-permanent).

> This includes new executive management and support positions as well as seven additional positions to pursue a more robust enforcement program.

The proposed 2011 staffing authorization also includes additional permanent attorney and support staff positions in the Legal Division to address higher consumer protection supervision and enforcement workload levels.

Resolutions and Receivership Management

Consistent with the expected decline in the number of insured institution failures in 2011, the proposed 2011 Corporate Operating Budget reflects a net reduction of 133 positions in authorized DRR staffing. This includes a decrease of 251 authorized non-permanent positions, which would be partially offset by a proposed increase of 118 authorized permanent positions. The increase in authorized permanent staffing reflects a proposed expansion in DRR's permanent staffing platform to ensure future readiness. If approved, DRR would have a permanent staffing platform of 412 positions plus a variable component to provide a continuing pipeline of trainees from DRR's three-year commissioning program.[6] An inability to successfully address all insured institution failures is perhaps the FDIC's most significant reputational risk, and DRR's permanent staffing platform is the key component in ensuring the Corporation's readiness.

At the beginning of 2007, DRR's permanent staffing authorization was only 223 (it has since been increased to the current 324). The proposed increase reflects a determination that DRR's permanent staffing platform did not provide adequate readiness at the outset of the current financial crisis to address the workload associated with the resolution of failed insured depository institutions while the Corporation added temporary staff to address increasing failure-related workload. DRR management conducted an in-depth review of its permanent staffing requirements, based upon the judgment of DRR managers about the level of staffing that was needed in each functional area to meet ongoing workload requirements until temporary staffing could be added as failure-related workload increased. The proposed new permanent staffing authorization is based upon the maintenance of readiness to address 12-25 insured institution failures per year.

DRR's internal analysis was recently reviewed and validated by an independent, outside consulting firm engaged by the CFO to conduct a comprehensive review of permanent DRR and Legal Division platform staffing requirements. The purpose of that review was to ensure that the Corporation was prepared to respond with its permanent staff to sudden and unexpected upticks in failure activity until additional non-permanent employees and contractors could be brought on board to assist with the increased workload.

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[6]Under DRR's proposal, commissioned Resolutions and Receivership Specialists would fill all permanent CG-9/13 Resolutions and Receivership Specialist vacancies in both the Washington and Dallas offices as they occurred. Trainees would be assigned to vacant positions within the permanent staffing platform as they completed the commissioning program. The number of authorized trainee positions would be adjusted annually to reflect actual DRR attrition from these positions (initially sized at 10 trainees per year, or a total of 30 positions in the commissioning program).

Monitoring and Resolution of Systemically Important Financial Companies

CFI was established to fulfill the Corporation's new responsibilities under the Dodd-Frank Act to monitor large, systemically important financial companies and to review the resolutions plans they submit. CFI will focus on systemically important bank holding companies and non-bank financial companies with more than $100 billion in assets. The proposed 2011 budget includes authorized staffing of 156 positions (all permanent) for CFI to perform these functions. This is a net increase of 121 positions over initial 2010 authorized staffing levels (35 authorized positions were transferred from DSC to CFI in conjunction with the establishment of CFI).

Most of the new positions will be devoted to the monitoring of approximately 20 bank holding companies and an indeterminate number of systemically important non-bank financial companies designated by the Financial Stability Oversight Council. This will include monitoring of individual institutions as well as cross-institutional (horizontal) monitoring. A large number of positions will also be dedicated to the review of resolution plans submitted by these companies and to the establishment of effective international and cross-border relationships.

Continuation of Staffing Flexibility Authority

In conjunction with its approval of proposed 2010 staffing authorizations in December 2009, the Board approved a proposal to provide all divisions and offices on a pilot basis with limited flexibility to temporarily exceed their permanent staffing authorizations in order to address succession management and other human capital concerns. The key elements of that proposal were as follows:

- Each division and office was granted the authority to exceed its permanent staffing authorization by up to 2 percent at any point during the year (the average annual attrition rate for most divisions and offices).[7] A specific numerical cap on this authority was established by the CFO for each division and office at the beginning of 2010.

- The CFO was delegated the authority to approve requests for a cap higher than 2 percent for a division or office if that organization was fully staffed up to the 2 percent limit and could demonstrate to the CFO, using objective quantitative data and analysis, that its attrition was likely to exceed two percent during the coming year because of projected retirements[8] or other known factors.

- If an organization's current permanent staffing was already more than 2 percent above its permanent staffing authorization due to previously-approved "temporary over-hire" or

[7]For DSC (now RMS and DCP), this authority was based on its permanent, *non-examiner* staffing authorization, excluding all authorized permanent non-supervisory field examiner positions.
[8]Requests based on retirement projections were required to utilize the projections in the most conservative scenario in the Division of Finance's annual *FDIC Retirement Analysis*.

> "incumbency only" authority, that organization was permitted to temporarily exceed the 2 percent limit until its excess permanent staffing dropped below 2 percent as the result of attrition from positions designated to be abolished under the current "temporary over-hire" or "incumbency only" authorities.

The pilot staffing flexibility program was successful in 2010, and we propose that it be continued on a permanent basis beginning in 2011. If approved, and absent approval from the CFO for higher limits in certain organizations, this program would permit the corporate-wide "over-hiring" of no more than 76 permanent employees nationwide above authorized 2011 permanent staffing levels.

Overview of Attached Exhibits

Attachment 1 displays the proposed 2011 Corporate Operating Budget by major expense category. Attachment 2 displays the proposed 2011 Corporate Operating Budget by division and office. Attachments 3 and 4 display the proposed budget by division/office for the two separate budget components (ongoing operations and receivership funding). Attachment 5 shows the projected allocation of the proposed budget by major program and fund. Attachment 6 shows proposed 2011 authorized staffing levels (permanent and non-permanent) for each division and office. Attachment 7 provides estimates of 2011 spending for the active investment project for which a separate investment project budget has been previously approved by the Board (those estimated expenses are not included in the proposed 2011 Corporate Operating Budget).

Also attached is the proposed 2011 Budget Resolution.

Contact Information

If you have questions or need additional information, please contact Thomas E. Peddicord, Deputy Director, Division of Finance, at (703) 562-6252.

Attachments