



Office of Inspector General

Statement

Subcommittee on Financial Services and
General Government
Committee on Appropriations
U.S. Senate

Office of Inspector General Fiscal Year 2008 Appropriation Request

Statement of Jon T. Rymer
Inspector General

Mr. Chairman and Members of the Subcommittee:

I am pleased to present the fiscal year 2008 budget request totaling \$26.8 million for the Office of Inspector General (OIG) at the Federal Deposit Insurance Corporation (FDIC), the first budget request since I took office on July 5, 2006. This request will allow us to continue meeting our statutory responsibilities and assist the FDIC in effectively carrying out its mission.

As you know, the Congress created the FDIC in 1933 as an independent executive agency, during the Great Depression, to maintain stability and public confidence in the nation's banking system. Our nation has weathered several economic downturns since that era without the severe panic and loss of life savings unfortunately experienced in those times. The federal deposit insurance offered by the FDIC is designed to protect depositors from losses due to failures of insured commercial banks and thrifts. The Congress enacted deposit insurance reform legislation that will maintain insurance coverage for individual accounts at \$100,000, but provides for inflation indexing every 5 years beginning in 2011. Also, as of April 1, 2006, coverage for certain retirement accounts increased to \$250,000 from \$100,000, with similar inflation indexing. According to most recent FDIC data, as of December 31, 2006, the FDIC insured \$6.6 trillion in deposits for 8,693 institutions, of which the FDIC supervised 5,220. The FDIC promotes the safety and soundness of these institutions by identifying, monitoring, and addressing risks to which they are exposed.

The Corporation reports that industry earnings are at record-high levels, bank capital is historically high, and loan performance has slipped only slightly from record levels. Currently, there are 50 institutions on the "problem list" – one of the lowest numbers in the history of the FDIC. Unfortunately, the 31-month streak of no failures – the longest in FDIC history – ended in February 2007, when one small institution, Metropolitan Savings Bank, failed. Still, the financial health of the banking industry remains very good overall. As for the economy, it is now in a sixth year of expansion; however, U.S. economic growth appears to be slowing significantly and some negative trends are emerging in the banking sector. They include a narrowing of net interest margins; increasing concentrations of riskier commercial real estate loans; and signs of credit distress in subprime mortgage portfolios. As economic conditions shift, the OIG is poised to focus its work on the challenges facing the FDIC in monitoring and assessing various existing and emerging risks to insured depository institutions and the Deposit Insurance Fund.

The FDIC OIG is an independent and objective unit established under the Inspector General Act of 1978, as amended. The OIG's mission is to promote the economy, efficiency, and effectiveness of FDIC programs and operations, and protect against fraud, waste, and abuse to assist and augment the FDIC's contribution to stability and public confidence in the nation's financial system.

Before discussing our budget needs for fiscal year 2008, I would like to highlight some of our accomplishments from the past fiscal year, our assistance to FDIC management, our planning and internal initiatives to improve the OIG, and the management and performance challenges facing the FDIC.

A Review of the FDIC OIG's FY 2006 Accomplishments

As in past years, during fiscal year 2006, our work in audits, evaluations, and investigations resulted in a number of major achievements, as follows:

- \$44.9 million in actual and potential monetary benefits
- 26 audit and evaluation reports issued
- 82 non-monetary recommendations to FDIC management
- 49 referrals to the Department of Justice

- 42 indictments/informations
- 26 convictions
- 1 employee/disciplinary action

More specifically, our accomplishments included investigations that led to the above indictments and convictions as well as fines, court-ordered restitution, and recoveries that constitute slightly over \$39 million in actual and potential monetary benefits from our work. Our audit and evaluation reports included about \$3.4 million in questioned costs and \$1.5 million in recommendations that funds be put to better use. The audit and evaluation reports contained non-monetary recommendations to improve FDIC policies, operations, and controls that ultimately are designed to improve the FDIC's ability to effectively and efficiently accomplish its mission.

On the whole, the OIG accomplished all of its organizational goals during the fiscal year, as outlined in our annual performance plan. Our 2006 Performance Report shows that we met or substantially met 100 percent of our goals. In a measurable way, this achievement shows the progress we continue to make in adding value to the Corporation with our audits, investigations, and evaluations in terms of impact, quality, productivity, and timeliness.

The following audit, evaluation, and investigative work illustrates some of the OIG's accomplishments in fiscal year 2006:

- Audit reports addressed significant issues. For example, one report contained recommendations to ensure that the FDIC periodically validates key assumptions, estimates, or other components that factor into the calculation of the reserve ratio, which is the ratio of the balance in the Deposit Insurance Fund to estimated deposits in the banking system. In connection with corporate governance practices, this report also recommended improved communication of information relevant to deposit insurance assessment determinations and other corporate matters and activities to the FDIC Board of Directors. Several reports dealt with various consumer protection and community reinvestment issues, including predatory lending, use of Home Mortgage Disclosure Act data to identify and assess instances of potential discrimination in FDIC-supervised institutions, and the FDIC's process for addressing the violations and deficiencies reported in compliance examinations. Our Federal Information Security Management Act-related audits have contributed to the FDIC making significant progress in the past several years in improving security controls and addressing current and emerging information security requirements.
- Evaluation reports focused on a number of important corporate issues, including the industrial loan company application process, the FDIC's safeguards over personal information, contract administration, and the FDIC's emergency response plan. The reports have generally contributed to strengthened program controls and improved corporate governance of FDIC operations.

Successful investigative outcomes included the following:

- The former president and chief executive officer of Hawkeye State Bank (HSB) was ordered to pay \$3.7 million in restitution based on his stipulating to having caused \$4.9 million in losses to HSB. He was sentenced to 65 months of incarceration and 5 years of supervised release.
- The former president of the First National Bank of Blanchardville was sentenced to 9 years' incarceration and ordered to pay restitution of \$13 million to the FDIC.
- The former chairman of the board and chief executive officer of Hamilton Bank was sentenced to 30 years of incarceration and 36 months of supervised released. He had earlier been convicted on all 16 charges of making false filings to the Securities and Exchange Commission and to bank examiners,

making false statements, wire fraud, bank fraud, securities fraud, obstruction of a bank examination, and conspiracy. He, along with two other convicted Hamilton Bank officers, was ordered to pay \$32 million in total restitution for bank and securities fraud, \$16 million of which is payable to the FDIC.

- The former chief executive officer (CEO) of the now defunct Sunbelt Savings and Loan of Dallas, Texas, an institution whose insolvency cost taxpayers approximately \$1.2 billion, was sentenced to 15 years' imprisonment and ordered to pay a criminal forfeiture of \$2.0 million to the United States Government and restitution in the amount of \$312,828 to the FDIC. The former CEO was convicted on 27 counts involving defrauding the FDIC of its payments of \$7.5 million and \$8.5 million in a civil judgment resulting from his 1990 guilty plea to federal fraud charges in connection with the collapse of Sunbelt.

Assistance to FDIC Management

In addition to audits, investigations, and evaluations, the OIG made valuable contributions to the FDIC in several other ways. Among these contributions were the following activities:

- Reviewed 14 proposed corporate policies and offered comments and suggestions when appropriate (e.g., Employee Rights and Responsibilities under the Privacy Act of 1974, Encryption and Digital Signatures for Electronic Mail, Protection of Privacy Information, the FDIC's Software Configuration Management Program, and Enterprise Risk Management);
- Participated in division-level conferences and meetings to communicate our audit, evaluation, and investigation work and processes;
- Provided technical assistance and advice to several FDIC groups working on information technology issues, including participating at the FDIC's information technology security meetings;
- Reviewed and/or commented on four draft legislative documents and regulations.

We are committed to continuing to demonstrate to the Congress, the public, the FDIC, and the banking industry that the OIG is doing the right things and generating results that are a worthy return on the investment made in us.

OIG Planning and Internal Initiatives

In fiscal year 2006, we undertook a comprehensive and integrated approach to planning OIG audits, evaluations, investigations, and internal activities, resulting in a Business Plan that captures our strategic goals, performance goals, and key efforts. We have been planning, conducting our work, and reporting our results in the context of these strategic goals since that time and will continue to do so in fiscal years 2007 and 2008. The OIG's work is centered on five strategic goals that link directly to the FDIC's mission, principal business lines, and significant challenges: Supervision, Insurance, Consumer Protection, Receivership Management, and Internal Resources Management. To these, we added a goal related to our internal processes in the interest of continuing to build and sustain a high-quality OIG work environment. We are pursuing that goal intently through a number of operational improvement projects.

These projects include professional development; human capital management and leadership development; client, stakeholder, and staff relationships; quality and efficiency of OIG work; strategic and annual performance planning and measurement; and information technology. These initiatives are

important for the OIG to ensure that we build and sustain the quality of our work and remain a results oriented high-performance organization, use our resources wisely, and stay abreast of the significant and ever-changing challenges facing the FDIC and the financial services industry.

The complete *2007 Business Plan* can be found on our Web page at <http://fdicig.gov> or obtained by contacting our office. Consistent with our working *Business Plan*, we are currently developing performance goals and key efforts for fiscal years 2008 and 2009, which will continue building on our six strategic goals. We will also continue to coordinate closely with the Congress, FDIC management, financial regulatory OIGs, others in the IG community, the U.S. Government Accountability Office, and law enforcement agencies as we plan and conduct our upcoming work.

Management and Performance Challenges Facing the Corporation

As part of our planning and budgeting process, the OIG annually assesses the most significant management and performance challenges facing the Corporation, in the spirit of the Reports Consolidation Act of 2000. In identifying those challenges, we consider the FDIC's strategic goals and the Chairman's corporate priorities and objectives. Identifying these challenges helps guide our work. In February 2007, we identified the following management and performance challenges facing the Corporation for inclusion in the Corporation's Performance and Accountability Report: addressing risks in large banks; maintaining strong regulatory capital standards; implementing deposit insurance reform; maintaining an effective examination and supervision program; granting insurance to and supervising industrial loan companies; guarding against financial crimes in insured institutions; safeguarding the privacy of consumer information; promoting fairness and inclusion in the delivery of information, products, and services to consumers and communities; ensuring compliance with consumer protection laws and regulations and follow-up on violations; being ready for potential institution failures; and promoting sound governance and managing and protecting human, financial, information technology, physical, and procurement resources.

FDIC Chairman Bair recently expressed her views on several challenges that the Corporation is facing and that she believes will continue to warrant attention over the next few years. The Chairman highlighted the following challenges as "front-burner" issues:

- Making sure the FDIC has a strong, vigilant supervisory program and creating a strong interrelationship between compliance and risk management;
- Implementing deposit insurance reform to help ensure a deposit insurance pricing system that reinforces the supervisory program;
- Maintaining strong regulatory capital standards under Basel II;
- Granting insurance to and supervising industrial loan companies;
- Promoting fairness and inclusion in the delivery of information, products, and services to consumers and communities; and
- Promoting sound governance and managing resources.

In addition to these priorities, Chairman Bair recently testified before the House Subcommittee on Financial Institutions and Consumer Credit of the Committee on Financial Services regarding other

management and performance challenges facing the Corporation. Chairman Bair focused on the following:

- Strengthening protections available to borrowers in the subprime mortgage market; and
- Ensuring that predatory lending practices do not take root in the banking system.

Clearly, our assessment of corporate challenges and the Chairman's articulation of priority issues are closely aligned. We look forward to continuing to work with the Congress and corporate officials to address all of these challenges successfully.

OIG's Fiscal Year 2008 Request

Our fiscal year 2008 budget request seeks the resources necessary to allow the OIG to continue its efforts in audit, investigative, and evaluation work. In addition, our funding allows us to continue to enhance knowledge capacity, employee programs, and operational improvement projects. These funds are essential to helping us remain prepared to meet the complex issues and challenges confronting the FDIC. The funds are critical to ensure that OIG can continue to provide our clients with timely, objective, and reliable information on how well FDIC programs, operations, and policies are working, and, when needed, recommendations for improvement. The OIG is an invaluable tool for helping the FDIC protect against fraud, waste, and abuse to assist and augment the Corporation's contribution to stability and public confidence in the nation's financial system.

At this time, we anticipate handling a 2008 investigative workload comparable to that of 2007. With respect to 2008 audit and evaluation work, we also anticipate a similar level of effort, with sustained attention to many of the Chairman's corporate priorities. Some key efforts begun in fiscal year 2007 will carry over into fiscal year 2008. To remain responsive to ever-changing priorities and emerging issues, we will keep close track of our planned work and make adjustments, as needed, to maximize the value that we add.

After 11 years of consecutive budgetary decreases, our fiscal year 2008 budget request in the amount of \$26,848,000 represents a modest increase of \$592 thousand (or 2.2 percent) over our fiscal year 2007 funding level. This budget request reflects a stabilized OIG operating environment and will support a full-time equivalent staff of 127, down 3 from fiscal year 2007. Even with the reduction in staffing, the slight increase in budget is required to help absorb higher projected expenses for employee salaries and benefits costs and non-personnel related expenses. As in past years, funds for the OIG budget would be derived from the Deposit Insurance Fund and the Federal Savings and Loan Insurance Corporation Resolution Fund.

Concluding Remarks

I appreciate the support and resources we have received from this Subcommittee, the Congress, and the FDIC. As a result, the OIG has continued to pursue successful investigations and to make a difference in FDIC operations in terms of financial benefits and improvements and strengthened internal operations and efficiency. I look forward to continue working with this Subcommittee in years to come. I believe our fiscal year 2008 budget strikes an appropriate balance between the mandate of the Inspector General Act, other legislative requirements, our judgments of OIG workload needs, and the changing conditions in the banking industry. We continue to seek your support so that we will be able to effectively and efficiently conduct our work on behalf of the Congress, the FDIC, and the American public.