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

December 12, 2008

TO: Board of Directors

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

SUBJECT: Proposed 2009 Corporate Operating Budget

Proposal

This memorandum requests that the Board of Directors approve the proposed 2009 Corporate Operating Budget totaling $2,243,765,244, including $1,243,765,244 for ongoing operations and $1,000,000,000 for receivership funding.[1] The total proposed 2009 Corporate Operating Budget is slightly over $1.0 billion (84.4 percent) higher than the approved 2008 Corporate Operating Budget, with most of the proposed increase in the receivership funding component of the proposed budget. The ongoing operations budget is approximately $177 million (16.6 percent) higher than the approved 2008 ongoing operations budget, while the proposed receivership funding budget is $850 million (567 percent) higher than the current 2008 receivership funding budget of $150 million approved by the Board in September 2008.

Approval is also requested for an authorized 2009 corporate staffing level of 6,269 (5,065 permanent, 1,204 non-permanent), up 548 positions from the currently-approved 2008 authorized staffing level of 5,721 (4,786 permanent and 935 non-permanent).

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 2009 Corporate Operating Budget have not yet been finalized. For example, the pool for 2009 pay increases 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 2009 Corporate Operating Budget. As in prior years, the proposed 2009 Budget Resolution delegates authority to the Deputy to the Chairman and Chief Financial Officer to adjust the total Board-approved 2009 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. In December 2007, the Board again approved a receivership funding budget of $75 million for 2008, but increased that budget to $150 million in September 2008 because of the increasing number of insured institution failures and the likelihood that actual 2008 expenses would substantially exceed $75 million.

2009 Workload Analysis and Projections

As in prior years, the proposed 2009 budget was formulated primarily on the basis of 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 by the Chairman and FDIC senior management 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. Workload projections were adjusted, as necessary, to be consistent with the "stress test" scenarios used to develop the Deposit Insurance Fund (DIF) restoration plan considered by the Board in October 2008. Under the proposed budget, the Corporation will focus largely on its core mission responsibilities in 2009 and will not devote significant resources to discretionary activities. These core mission responsibilities include fulfillment of all of the annual performance goals established in the Corporation's *2009 Annual Performance Plan*.

The number of FDIC-insured and supervised financial institutions is projected to continue to decline in 2009, but the Corporation's supervisory workload is nonetheless expected to increase. The proposed 2009 budget includes resources to conduct an estimated 2,473 risk management examinations of FDIC-supervised institutions (43 more than are now projected for 2008). However, in the current economic environment, these examination projections may well

[2] Salary and benefits expenses for the permanent in-house staff associated with the Corporation's Receivership Management business line (primarily in DRR 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.

fluctuate throughout 2009. The most important driver of the Corporation's projected 2009 risk management workload is the increasing number of institutions with composite CAMELS ratings of 3, 4, and 5. Examinations of such institutions require substantially more time than examinations of 1- and 2-rated institutions. In addition, based on the Corporation's experience in 2008, the FDIC expects to devote more time to back-up supervision activities related to problem institutions supervised by other Federal regulators. The FDIC has also increased its average benchmark hours for risk management examinations of 1- and 2- rated institutions for 2009. The increased time required for risk management examinations of these institutions is largely attributable to the increasing complexity of financial institution operations.

The proposed 2009 budget also includes the resources required to conduct 1,911 CRA and compliance examinations of FDIC-supervised institutions (131 more than are now projected for 2008). That increased workload reflects plans to accelerate the schedule for some examinations in order to distribute the compliance examination workload more evenly across years. In addition, as with risk management examinations, the FDIC has also increased its average benchmark hours for compliance examinations. The increased time required for compliance examinations is largely attributable to the inclusion of new regulatory requirements.

The Corporation's resolutions and receivership management workload during the second half of 2008 has been much higher than originally projected and is expected to remain at or above this level throughout 2009. Thus far, 25 FDIC-insured institutions have failed in 2008 with assets totaling approximately $372 billion (book value). In addition, the percentage of failed institution assets retained by the FDIC at resolution has increased substantially from the Corporation's experience in recent years. Even if the number of failures declines at some point during the next year, a substantial volume of asset management, asset sales, and receivership claims workload will remain. This residual workload is expected to extend well beyond 2009.

In addition, over the past two months, FDIC staff has been heavily engaged in a number of initiatives designed to address the credit and liquidity problems within the U. S. economy. These include temporary changes to the scope of the FDIC's deposit insurance program, establishment of the new Temporary Liquidity Guarantee Program, and support for the Treasury Department's Troubled Asset Relief Program. There has also been discussion of a possible FDIC role in a home loan modification initiative. However, it has been difficult to project the extent to which staffing or other resources will be required by the FDIC in 2009 to support these initiatives. Accordingly, a decision was made to include in the proposed 2009 Corporate Operating Budget unallocated contingency funding of $2.5 million for these purposes.[3]

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[3]If needed, these funds (and any corresponding staffing authorizations) may be allocated to the 2009 operating budgets of affected organizations by the Chief Financial Officer, in accordance with authority delegated under the proposed 2009 Budget Resolution.

Sources of Revenue

Over 99 percent of the funding for the 2009 Corporate Operating Budget is projected to come from the DIF, with the remainder paid from the FSLIC Resolution Fund (FRF). Receiverships will be billed for services provided by the Corporation in accordance with established service billing procedures. The total spending authorized by the proposed 2009 Corporate Operating Budget represents approximately 224 percent of the interest revenue and 20 percent of the combined interest and assessment revenue projected for the DIF in 2009. This is a significant change from the last several years, when operating budget spending totaled less than half of the DIF's interest revenue, and reflects the combined impact of increased spending, a lower DIF balance, and reduced DIF revenue.

2009 Budget Highlights

Overview of Proposed 2009 Budget by Component

The proposed 2009 Corporate Operating Budget totals $2,243,765,244, including $1,243,765,244 for ongoing operations and $1,000,000,000 for receivership funding (see Attachment 1). The proposed ongoing operations budget is approximately $177 million (16.6 percent) higher than the approved 2008 ongoing operations budget. The proposed receivership funding budget is $850 million (567 percent) higher than the current 2008 receivership funding budget of $150 million approved by the Board in September 2008 and $925 million (1,233 percent) higher than the receivership funding budget originally approved by the Board for 2008.

The most significant factor contributing to the proposed increase in the ongoing operations component is the projected increase in the Corporation's supervisory workload in 2009 and the planned staffing increases in the Division of Supervision and Consumer Protection (DSC) to address that workload. In addition, the proposed ongoing operations budget reflects proposed 2009 increases in the permanent staffing platform (paid from the ongoing operations component) of the Division of Resolutions and Receiverships (DRR). Although staffing authorizations for DSC, DRR, and other organizations were increased incrementally throughout 2008, the full budgetary impact of these staffing increases will be incurred in 2009. The proposed 2009 ongoing operations budget also includes increased funds for travel, office space, and equipment for these additional staff.

The most significant factor contributing to the proposed increase in the receivership funding component of the proposed budget is the expected continuation in 2009 of the recent high level of failure activity and related receivership management work. To address this workload, the proposed 2009 receivership funding budget provides substantially increased resources for contractor support as well as non-permanent increases in authorized staffing for DRR, the Legal Division, and other organizations. 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 major upticks in workload. The proposed budget for contractor support is approximately $687 million, up more than $600 million from 2008, and constitutes almost 70 percent of the proposed 2009 receivership funding budget. The proposed

2009 budget also provides additional funding for leased space and equipment for the additional FDIC staff and on-site contractors (to be housed primarily in an expanded Dallas Regional Office and the recently-approved temporary West Coast Satellite Office) and for travel associated with resolutions and receivership management activities.

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 2009 or the actual expenses that will be incurred in connection with those failures. The proposed 2009 receivership funding budget should not, therefore, be regarded as a highly reliable estimate of 2009 expenses for this budget component. The proposed 2009 receivership funding budget was modeled on the basis of actual expenses incurred in connection with failures during the first nine months of 2008 and the assumed continuation in 2009 of the elevated level of failure activity that has occurred in recent months, with a reasonable contingency amount added to address the possibility of even higher levels of failure activity and/or higher average costs to resolve future failures. If an elevated level of failure activity continues in 2009, the growing number of receiverships will have a substantial cumulative impact on total receivership funding expenses.

We are hopeful that the proposed receivership funding budget will be sufficient to cover 2009 resolutions and receivership management expenses, but will return to the Board to seek additional funding if we determine during the year that additional budget authority is needed. We will be reviewing actual and projected resolutions and receivership management workload on a continuing basis throughout 2009 and plan to update the Board on the status of the receivership funding budget as part of planned briefings to be conducted on the overall 2009 Corporate Operating Budget at the end of each quarter.

Overview of Proposed 2009 Budget by Major Expense Category

Attachment 1 itemizes the proposed 2009 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: Although personnel-related expenses continue to be the largest category of expenses in the proposed budget, the budget for contractor support increases substantially from 2008 because of the Corporation’s heavy reliance on contractor support to address its increased resolutions and receivership management workload:

- The proposed 2009 budget for Salaries and Compensation is about $935 million, which is $216 million (about 30 percent) higher than the 2008 Salaries and Compensation budget. This is attributable largely to the substantial planned increase in FDIC staffing in 2009. The Salaries and Compensation expense category represents about 66 percent of the proposed 2009 ongoing operations budget, 12 percent of the proposed 2009 receivership funding budget, and 42 percent of the overall proposed 2009 Corporate Operating Budget.

- The proposed 2009 budget for Outside Services-Personnel (contractor-provided services) is about $871 million, which is about $619 million (246 percent) higher than the 2008 budget. This is attributable primarily to the expanded resolutions and receivership management workload projected for 2009. The Outside Services-Personnel expense category represents about 15 percent of the proposed 2009 ongoing operations budget, 69 percent of the proposed 2009 Receivership Funding budget, and 39 percent of the overall proposed 2009 Corporate Operating Budget.

The remainder of the proposed 2009 Corporate Operating Budget consists of Travel expenses ($137 million), up about $63 million (86 percent) from 2008 due to the increased number of FDIC staff and projected inflation in travel and relocation costs; Buildings and Leased Space expenses ($121 million), up about $53 million (78 percent) from 2008 due to the need for additional office space to house new FDIC staff and contractors; Equipment expenses ($68 million), up about $11 million (18 percent) from 2008; Outside Services-Other expenses ($47 million), up about $21 million (81 percent) from 2008; and Other Expenses ($64 million), up about $44 million (212 percent) from 2008.

Proposed Funding for Major Corporate Initiatives

The proposed budget includes new funding in the budgets of the Executive Offices, Corporate University, and the Division of Information Technology for implementation of selected initiatives in the Culture Change Strategic Plan. Most of the proposed initiatives do not require additional resources. The proposed Corporate University budget includes funds for both additional staffing and contractual support to develop and implement a new leadership curriculum, one of the key recommendations of the Culture Change Council.

The proposed budget also includes additional staff and contractual support to address the major increase in deposit insurance inquiries that the Corporation has been experiencing since mid-2008; modestly increased resources for economic inclusion and community outreach programs; continued funding for *Money Smart* and other financial literacy initiatives; and continued funding for the foreclosure counseling and outreach activities being undertaken in partnership with NeighborWorks® America.

Overview of Proposed Increases in Authorized 2009 Staffing

Supervision

The proposed 2009 Corporate Operating Budget provides for another significant increase in authorized DSC staffing to address the Corporation's supervisory responsibilities (primarily field examination staff) beyond the increase approved for 2008. This increase is needed to address the expanding number of troubled FDIC-insured and supervised institutions, the changing nature of industry operations, and the increasing volume of regulatory requirements. Authorized 2009 DSC staffing is proposed to increase to 3,277 positions (2,901 permanent, 376 non-permanent), an increase of 425 positions in DSC's currently-authorized staffing level and 552 positions more than the 2008 DSC staffing level originally approved by the Board. This includes 2,161 field examination staff (1,836 permanent, 325 non-permanent),[4] an increase of 353 positions from the currently-authorized field examination staffing level and 473 positions from the examination staffing level originally approved by the Board for 2008. The 2,161 field examination positions are comprised of 1,723 risk management examination positions (1,447 permanent, 276 non-permanent) and 438 compliance examination positions (389 permanent, 49 non-permanent).

The proposed DSC staffing authorization also includes additional supervisory examiners, case managers, and other positions to address the elevated supervision workload. Where the workload increase is expected to be temporary, the additional positions are proposed on a non-permanent basis. A small increase in Legal Division staff is also proposed to provide expanded support for the supervision function. DSC and Legal Division staff have recently been devoting considerable time to supervision-related activities in support of TARP and the TLGP; however, no staffing or other resources requirements have yet been identified for these programs until the scope and duration of this additional workload becomes clearer.

Resolutions and Receivership Management

The proposed 2009 Corporate Operating Budget provides for significant increases in authorized staffing in DRR and the Legal Division to address the Corporation's elevated resolutions and receivership management workload. Most of the staffing increases are proposed to be non-permanent. However, an increase of 61 positions is proposed in DRR's permanent staffing platform, because the permanent staffing platform established by DRR in 2005 has proven to be inadequate to deal with the significant increase in failure activity that the FDIC has experienced over the past year.[5] Authorized 2009 DRR staffing is proposed to increase to 847 positions (284 permanent, 563 non-permanent). This is only 22 positions above DRR's currently-authorized 2008 staffing level, because DRR's staffing authorization has been increased on an incremental basis throughout the past eight months to address the rising number of failures and near failures.[6] But, the proposed 2009 staffing authorization is 624 positions higher than the 2008 DRR staffing level of 223 (all permanent) originally approved by the Board, representing a 280 percent increase in authorized DRR staffing over a one-year period.

The proposed DRR staffing increase is composed largely of additional resolutions and receivership specialist positions in a wide variety of functional specialties, including deposit claims, franchise and asset marketing, asset management and sales, and investigations. In addition, the proposed 2009 Legal Division staffing authorization includes about 200 new positions that have been added since the beginning of 2008 to provide legal support for the higher levels of resolutions and receivership management activity.

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[4]The 2,161 authorized field examination positions exclude 120 entry-level field examiner trainee positions in Corporate University.

[5]The Corporation plans to undertake in early 2009 a comprehensive review of permanent DRR staffing requirements in order to ensure that its staffing is adequate to deal with future banking crises without being dependent on staff detailed from DSC.

[6]These staffing increases were approved by the Chief Financial Officer, in consultation with the Chairman and members of the Board, in accordance with authority delegated to him by the Board in the 2008 Budget Resolution.

Projected Investment Budget Spending

In December 2002, the Board established an Investment Budget that was separate and distinct from the annual corporate operating budget. The Investment Budget consists of individual investment project budgets that are separately approved by the Board (prior to 2003, funding for such projects was included in the Corporation's annual corporate operating budgets). These projects are funded on a multi-year basis, and the funds approved by the Board cannot be reprogrammed among projects or for any other purpose. The Capital Investment Review Committee (CIRC) monitors the progress of approved investment projects and reports on them quarterly to the Board.

The Investment Budget currently includes only three active information technology (IT) projects, and one of them (4C, formerly the Asset Servicing and Technology Enhancement Project) is already operational and has been largely completed. Investment Budget spending has declined from a high of about $108 million in 2004 (when there were 10 approved investment projects underway) to an approximately $25 million in 2008. Investment Budget spending is projected to be approximately $4 million in 2009.

Overview of Attached Exhibits

Attachment 1 displays the proposed 2009 Corporate Operating Budget by major expense category. Attachments 2 and 3 display the proposed budget by division/office for the two separate budget components (ongoing operations and receivership funding). Attachment 4 shows the projected allocation of the proposed budget by major program and fund. Attachment 5 shows proposed 2009 authorized staffing levels (permanent and non-permanent) for each division/office.

Also attached is the proposed 2009 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