Federal Deposit Insurance Corporation
550 17th Street, NW, Washington, DC 20429

December 7, 2009

TO: Board of Directors

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

SUBJECT: Proposed 2010 Corporate Operating Budget

Proposal

This memorandum requests that the Board of Directors approve the proposed 2010 Corporate Operating Budget totaling $3,989,279,789, including $1,489,279,789 for ongoing operations and $2,500,000,000 for receivership funding.[1] The total proposed 2010 Corporate Operating Budget is about $1.4 billion (55.8 percent) higher than the approved 2009 Corporate Operating Budget, with most of the proposed increase in the receivership funding component of the proposed budget. The ongoing operations budget is approximately $230 million (18.2 percent) higher than the approved 2009 ongoing operations budget, while the proposed receivership funding budget is $1.2 billion (92.3 percent) higher than the 2009 receivership funding budget of $1.3 billion.[2]

Approval is also requested for a total authorized 2010 corporate staffing level of 8,653 (5,232 permanent, 3,421 non-permanent), up 1,643 positions from the currently-approved 2009 authorized staffing level of 7,010 (5,148 permanent, 1,862 non-permanent). This includes approval of individual division and office staffing authorizations, with limited flexibility for divisions and offices to exceed temporarily their permanent 2010 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.

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[1]Certain factors that affect the Salaries and Compensation category of the proposed 2010 Corporate Operating Budget have not yet been finalized. For example, the Corporation is currently engaged in compensation negotiations with the National Treasury Employees Union that will determine locality pay rates as well as the cost of several other components of employee pay and benefits for 2010. When these factors are finally determined, they may require corresponding changes in estimated expenses for the Salaries and Compensation major expense category of the 2010 Corporate Operating Budget. As in prior years, the proposed 2010 Budget Resolution delegates authority to the Deputy to the Chairman and Chief Financial Officer to adjust the total Board-approved 2010 Corporate Operating Budget to account for such factors.

[2]This assumes approval by the Board of Directors of a proposed $300 million increase in the 2009 receivership funding budget component, which is scheduled to be considered by the Board at its meeting on December 15, 2009.

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 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.[3] 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 an unexpected increase in the number of insured institution failures and the likelihood that actual 2008 expenses would substantially exceed $75 million. In 2009, a $1.0 billion receivership funding budget was initially approved by the Board, but a proposed increase in that budget to $1.3 billion is currently pending approval.

2010 Workload Analysis and Projections

As in prior years, the proposed 2010 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. The same workload projections have been used in the formulation of both the proposed 2010 Corporate Operating Budget and the assessment rate case and analysis that was presented to the Board in September 2009. During 2010, the Corporation will continue to focus largely on its core mission responsibilities 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 *2010 Annual Performance Plan*.

[3]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.

The Corporation's projected supervision and resolutions/receivership management workload are the primary determinants of the resource requirements reflected in the proposed 2010 budget, and workload in both areas is expected to be even higher in 2010 than it has been in 2009. The proposed 2010 budget includes resources to conduct an estimated 2,532 risk management examinations and 1,900 Community Reinvestment Act and compliance examinations of FDIC-supervised institutions, both down slightly from 2009 due to failures and consolidation within the banking industry. But, the most important driver of the Corporation's supervision workload is the large 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. The number of 3-, 4-, and 5-rated institutions has increased by over 80 percent thus far during 2009 and is expected to continue to increase next year. The FDIC also performs back-up supervisory activities related to problem institutions supervised by other Federal regulators, and the number of those institutions has also increased in a similar fashion.

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 management work it is managing. Both are expected to be higher in 2010 than they have been in 2009. There have been 130 failures of FDIC-insured depository institutions thus far in 2009, and the proposed 2010 budget will ensure that the Corporation is prepared, if necessary, to handle an even larger number of failures next year. Assuming continued high levels of failure activity in 2010, the Corporation's post-failure receivership management workload will also continue to rise next year from current levels. The FDIC is now managing 177 active receiverships emanating from insured institution failures, and the Corporation's inventory of assets in liquidation has risen from approximately $15.1 billion (book value) at the beginning of 2009 to $36.8 billion (book value) as of November 30, 2009. The Corporation is also overseeing 81 active loss share agreements involving closed banks, with additional assets totaling approximately $108 billion (book value). Even when the number of institution failures begins to decline at some point in the future, a substantial volume of residual receivership management workload (asset management, asset sales, receivership claims, etc.) will continue well beyond 2010.

2010 Budget Highlights

Overview of Proposed 2010 Budget by Component

As noted above, the proposed 2010 Corporate Operating Budget totals $3,989,279,789, including $1,489,279,789 for ongoing operations and $2,500,000,000 for receivership funding (see Attachment 1). The most significant factor contributing to the proposed increase in the ongoing operations component is the projected increase in the Corporation's supervision workload in 2010, which will require further staffing increases in both the Division of Supervision and Consumer Protection (DSC) and the Legal Division. These staffing increases will result in higher spending for salaries and benefits, travel, office space, equipment, and other expenses. The proposed 2010 ongoing operations budget includes an unallocated contingency reserve of $15 million (approximately 1 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. A $2.5 million contingency reserve was included in the 2009 ongoing operations budget, but proved inadequate to meet all of the additional funding requirements that arose during the year.

The most significant factor contributing to the proposed increase in the receivership funding component of the proposed budget is the expected high level of failure activity and post-failure receivership management workload next year. This workload will require further increases in both staffing and contractor resources in the Division of Resolutions and Receiverships (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 temporary upticks in workload. The proposed budget for contractor support is approximately $1.8 billion, up nearly $950 million from 2009, and constitutes 72.5 percent of the proposed 2010 receivership funding budget. The proposed 2010 receivership funding budget also includes additional funding for travel, leased space and equipment to support the higher number of FDIC employees and contractors and an unallocated contingency reserve of slightly more than $175 million (7.0 percent of the proposed receivership funding budget) to be administered by the CFO to meet unbudgeted resource requirements that arise during the year. Approximately $64 million in unallocated contingency funds were included in the 2009 receivership funding budget.

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 2010 or the actual expenses that will be incurred in connection with those failures. The proposed 2010 receivership funding budget should not, therefore, be regarded as a highly reliable estimate of 2010 expenses for this budget component. Based upon what is known today, we believe that the proposed receivership funding budget will be sufficient to cover 2010 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 resolutions and receivership management workload on a continuing basis throughout 2010 and plan to continue quarterly briefings for the Board on supervision and resolutions/receivership management workload trends.

Overview of Proposed 2010 Budget by Major Expense Category

Attachment 1 itemizes the proposed 2010 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 budget for contractor support increases substantially from 2009 because of the Corporation's reliance on contractor support to address much of its resolutions and receivership management workload.

- The proposed 2010 budget for Salaries and Compensation is about $1.3 billion, which is $354 million (about 38.2 percent) higher than the 2009 Salaries and Compensation budget. This is attributable largely to the substantial planned increase in FDIC staffing in 2010 and to the fact that the Corporation will incur full-year salary and benefits expenses for the more than 1,700 new employees were hired throughout the year during 2009. The Salaries and Compensation expense category represents 64.9 percent of the proposed 2010 ongoing operations budget, 12.6 percent of the proposed 2010 receivership funding budget, and 32.1 percent of the overall proposed 2010 Corporate Operating Budget.

- The proposed 2010 budget for Outside Services-Personnel (contractor-provided services) is about $2.1 billion, which is about $1.0 billion (94.7 percent) higher than the 2009 budget. This increase will ensure the Corporation's readiness to handle, if necessary, substantially increased resolutions and receivership management workload in 2010. The Outside Services-Personnel expense category represents about 16.5 percent of the proposed 2010 ongoing operations budget, 72.3 percent of the proposed 2010 Receivership Funding budget, and 51.5 percent of the overall proposed 2010 Corporate Operating Budget.

The remainder of the proposed 2010 Corporate Operating Budget consists of Travel expenses ($149.8 million), up about $9.2 million (6.6 percent) from 2009, due largely to increased staffing levels in DSC; Buildings and Leased Space expenses ($230.5 million), up about $13.8 million (6.3 percent) from 2009, to address increased office space requirements, including those associated with potentially higher levels of failure activity in 2010; Equipment expenses ($150.9 million), up about $36.8 million (32.2 percent) from 2009, to support the increased number of FDIC employees and contractors planned for resolutions and receivership management activities; Outside Services-Other expenses ($44.6 million), up about $2.4 million (5.8 percent) from 2009 due to increased receivership activity; and Other Expenses ($76.2 million), up about $13.4 million (21.4 percent) from 2009, primarily to cover higher administrative, training, and other expenses related to the projected increase in the number of FDIC employees and receiverships.

Overview of Proposed Increases in Authorized 2010 Staffing

Supervision

The proposed 2010 Corporate Operating Budget provides for further increases in authorized staffing in both DSC and the Legal Division to address the Corporation's supervisory responsibilities beyond the increases that were approved for 2009. These staffing increases are required to address the large number of troubled FDIC-insured and supervised institutions and the changing nature of industry operations. Authorized 2010 DSC staffing is proposed to increase to 3,780 positions (2,982 permanent, 798 non-permanent), an increase of 391 positions from 2009. This includes 2,459 field examination staff (1,836 permanent, 623 non-permanent), an increase of 298 positions from currently-authorized field examination staffing levels.[4] The proposed 2010 staffing authorization also includes additional supervisory examiners and case

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[4]The 2,459 authorized field examination positions do not include 120 entry-level field examiner trainee positions in Corporate University. The 2,459 positions are comprised of 2,014 risk management examination positions (1,447 permanent, 567 non-permanent) and 445 compliance examination positions (389 permanent, 56 non-permanent).

managers in DSC as well as additional attorneys and support staff in the Legal Division to address higher supervision and enforcement workload levels. Because the elevated level of supervisory workload is expected to be temporary, most of the additional DSC and Legal Division positions are proposed on a non-permanent basis.

Resolutions and Receivership Management

The proposed 2010 Corporate Operating Budget provides for significant increases in authorized staffing in DRR and the Legal Division to address potentially elevated resolutions and receivership management workload. Most of the staffing increases are proposed to be non-permanent. Authorized 2010 DRR staffing is proposed to increase to 2,310 positions (324 permanent, 1,986 non-permanent).[5] This is an increase of 954 positions (39 permanent, 915 non-permanent), 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. The proposed 2010 Legal Division staffing authorization includes 154 new positions for attorneys and support staff to help address the increasing legal workload that is expected next year in connection with the Corporation's resolutions and receivership management functions.

Staffing Flexibility Proposal

In conjunction with its approval of the proposed 2010 staffing authorizations, we are also requesting that the Board provide all divisions and offices with some limited flexibility to temporarily exceed their permanent staffing authorizations for 2010 in order to address succession management and other human capital concerns. The Board has previously approved "temporary over-hire" authority for selected divisions to address their high levels of projected retirements, but accounting for and tracking those special authorizations has resulted in substantial administrative burden. Several other divisions have requested similar special hiring authorities in 2010. Rather than adopt a variety of new, customized arrangements for different organizations, we are proposing a corporate-wide solution to address the increasing concern about succession management throughout the FDIC. If approved by the Board, this proposal will be implemented on a pilot basis only in 2010. A recommendation will be made to the Board in conjunction with the presentation of the proposed 2011 Corporate Operating Budget on whether to continue this approach in 2011 and future years.

The key elements of this proposal are as follows:

- Each division and office would be granted the authority to exceed its permanent staffing authorization by up to 2 percent during the year (the average annual attrition rate for most

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[5]The Corporation is conducting a comprehensive review of permanent DRR and Legal Division platform staffing requirements in order to ensure the Corporation's readiness to respond to sudden and unexpected upticks in failure activity before additional employees and contractors can be brought on board to assist with the increased workload. That study is expected to be completed in early 2010. At that time, the mix of permanent and non-permanent positions in the 2010 staffing authorizations for DRR and the Legal Division will be adjusted, as necessary, to be consistent with the study results.

divisions and offices).[6] A specific numerical cap on this authority would be established by the CFO for each division and office at the beginning of the fiscal year.

- The CFO would have the delegated authority to approve a request 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 2 percent during the coming year because of projected retirements[7] or other known factors.

- If an organization's current permanent staffing is already more than 2 percent above its permanent staffing authorization due to previously-approved "temporary over-hire" or "incumbency only" authority, that organization would be 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.

If approved, this proposal would provide divisions and offices with greater flexibility to address their succession management and knowledge transfer concerns and to devise solutions to other human capital issues that may be unique to their organizations. It would also reduce the administrative burden associated with the current tracking of "incumbency only" positions and could facilitate faster backfilling of vacant positions. Absent approval from the CFO for higher limits in certain organizations, this proposal would permit the corporate-wide "over-hiring" of no more than 68 permanent employees nationwide above authorized 2010 permanent staffing levels.

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 two active information technology (IT) projects. Investment Budget spending has declined from a high of about $108 million in 2004 (when there were 10 approved investment projects underway) to approximately $6.0 million in 2009.

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[6]For DSC, this authority is proposed to be based on its permanent, *non-examiner* staffing authorization, excluding all authorized permanent non-supervisory field examiner positions. If this proposal is approved, DSC would have the flexibility to hire up to 23 permanent employees above its authorized permanent staffing authorization in 2010 (total permanent staffing authorization of 2,982 less permanent field examiner staffing authorization of 1,836 equals 1,146; 23 is 2 percent of 1,146).

[7]Requests based on retirement projections would be required to utilize the projections in the most conservative scenario in the Division of Finance's annual *FDIC Retirement Analysis*.

Investment Budget spending is projected to be approximately $1.1 million in 2010 (see Attachment 7).

Overview of Attached Exhibits

Attachment 1 displays the proposed 2010 Corporate Operating Budget by major expense category. Attachment 2 displays the proposed 2010 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 2010 authorized staffing levels (permanent and non-permanent) for each division and office. Attachment 7 provides estimates of 2010 spending for the two active investment projects for which separate investment project budgets have been previously approved by the Board (those estimated expenses are not included in the proposed 2010 Corporate Operating Budget).

Also attached is the proposed 2010 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