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

November 27, 2012

TO: Board of Directors

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

SUBJECT: Proposed 2013 Corporate Operating Budget

Proposal

This memorandum requests that the Board of Directors approve the proposed 2013 Corporate Operating Budget totaling \$2,682,638,734, including \$1,782,638,734 for ongoing operations and \$900,000,000 for receivership funding.[1] The total proposed 2013 Corporate Operating Budget is \$598,139,911 (18.2 percent) lower than the approved 2012 Corporate Operating Budget, largely due to substantially reduced resource requirements for the receivership funding budget component. The proposed ongoing operations component of the budget is \$1,860,089 (0.1 percent) higher than the approved 2012 ongoing operations budget, while the proposed receivership funding component of the budget is \$600,000,000 (40 percent) lower than the 2012 receivership funding budget.

Approval is also requested for a total authorized 2013 corporate staffing level of 8,026 (5,833 permanent, 2,193 non-permanent), down 687 positions from the currently-approved 2012 authorized staffing level of 8,713 (5,835 permanent, 2,878 non-permanent). This includes approval of individual division and office staffing authorizations, with the same limited flexibility that has been provided in 2012 for individual divisions and offices to temporarily exceed their permanent 2013 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 2013 Corporate Operating Budget have not yet been determined (e.g., the Corporation's share of 2013 employee health insurance costs). When these factors are finally determined, they may require corresponding changes in estimated expenses for the Salaries and Compensation major expense category of the 2013 Corporate Operating Budget. As in prior years, the proposed 2013 Budget Resolution delegates authority to the Deputy to the Chairman and Chief Financial Officer to adjust the total Board-approved 2013 Corporate Operating Budget to account for such factors.

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 highly variable annual expenses associated with bank closings and subsequent receivership management 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 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 that 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, before declining to $2.202 billion in 2011 and $1.5 billion in 2012. By contrast, the ongoing operations component of the budget rose much more gradually during this period, from $1,032,489,659 in 2007 to $1,780,778,645 in 2012.

2013 Workload Analysis and Projections

During 2013, the Corporation will continue to focus on its historic mission responsibilities, including supervision of a large number of insured depository institutions (IDIs) in troubled or problem financial condition and the management of the large number of open receiverships established in conjunction with the failure of IDIs since 2008. But, substantial 2013 resources will also be devoted to fulfilling the Corporation's new responsibilities under the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (DFA), including monitoring the risks in large, systemically important financial institutions (SIFIs), reviewing the resolution plans submitted by companies covered by DFA, and preparing, if necessary, to undertake their orderly liquidation.

As in prior years, the proposed 2013 budget and staffing authorizations are based 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 planning and budget formulation process, and

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[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.

divisions and offices determined their budget requirements in accordance with that guidance. The Division of Insurance and Research (DIR) provides the Division of Risk Management Supervision (RMS), the Division of Depositor and Consumer Protection (DCP), and the Division of Resolutions and Receiverships (DRR) with semiannual updates to the industry analyses used in projecting key workload indicators.

The Corporation's projected supervision and resolutions and receivership management workload is the primary determinant of the resource requirements reflected in the proposed 2013 budget. The Corporation's supervision workload varies based upon the number and size of the institutions supervised by the FDIC and the number of those institutions with composite CAMELS (risk management) ratings of 3, 4, and 5. Those factors largely determine the number of risk management and compliance examinations to be conducted each year and the amount of examiner time spent on those examinations. [3] The primary drivers of the Corporation's resolutions and receivership management workload are the number of failures of FDIC-insured institutions, the number of active receiverships being managed by the FDIC, and the amount of post-failure workload remaining for those receiverships.

The number of FDIC-supervised institutions declined by 1,016 (18.4 percent), from 5,527 at year-end 2007 to 4,511 on October 31, 2012, due to bank failures and industry consolidation. Although the number of failures has dropped substantially since 2010, industry consolidation is expected to continue to reduce the number of FDIC-supervised institutions in 2013 and beyond. The reduction in the number of supervised institutions did not initially reduce the FDIC's supervision workload, because this factor was more than offset from 2007 through 2010 by the dramatic increase in the number of troubled and problem institutions that required more frequent and lengthy examinations and supervisory oversight. During 2011 and 2012, however, the number of 3-, 4-, and 5-rated institutions declined substantially (although it remains very high by historical norms) and is expected to continue a steady decline in 2013 and beyond, consistent with forecasts for a gradual economic recovery.

As a result, the number of risk management examinations will decline by a projected 4.1 percent from 2012 to 2013, from 2,669 to 2,559, and the total number of examination hours will decline by a projected 6.8 percent.[4] This will permit a significant decrease in the number of authorized non-permanent supervisory staffing for risk management in 2013, with continuing reductions in non-permanent risk management supervisory positions projected in 2014 and beyond. Compliance and CRA examination workload is less directly affected by unfavorable ratings and is projected to be relatively stable in 2013. The proposed 2013 Corporate Operating Budget includes the resources needed to conduct an estimated 1,729 compliance and CRA examinations, down 1.4 percent from 2012.

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[3]The projected number of compliance and Community Reinvestment Act (CRA) examinations to be conducted annually is based largely on the number of institutions supervised by the FDIC; compliance and CRA ratings have only a limited impact on this workload. DCP continues to manage the timing of scheduled examinations in accordance with Board-approved guidelines to mitigate substantial year-to-year variation in required examinations.
[4]The workload associated with enforcement activity will decline more slowly, particularly those enforcement activities related to individuals, because of the long timeframes associated with some types of enforcement actions.

The FDIC's resolutions and receivership management workload is also expected to decline substantially in 2013. The proposed budget is based on a continuing decline in the number of IDI failures in 2013, partially offset by an increase in the number of post-failure receiverships and loss share agreements being managed by the FDIC. There have been 50 failures of FDIC-insured depository institutions thus far in 2012, down from 92 in 2011, and the Corporation's inventory of assets in liquidation has fallen from approximately $20.9 billion (book value) at the beginning of 2012 to $17.8 billion (book value) on October 31, 2012. But, as of October 31, 2012, the Corporation was managing 468 active receiverships and overseeing 297 active loss share agreements emanating from insured institution failures, up from 431 receiverships and 278 loss share agreements at the beginning of 2012.[5] Moreover, a substantial amount of residual receivership management workload (asset management and sales, litigation, etc.) typically remains for several years beyond an institution's failure date.

2013 Budget Highlights

Overview of Proposed 2013 Budget by Component

The proposed 2013 Corporate Operating Budget totals $2,682,638,734, including $1,782,638,734 for ongoing operations and $900,000,000 for receivership funding (see Attachment 1). This represents an increase of $1,860,089 (0.1 percent) in the ongoing operations budget component and a decrease of $600,000,000 (40 percent) in the receivership funding budget component.

In the ongoing operations budget component, a projected 4.0 percent increase in the average salaries of most FDIC employees in 2013 will be largely offset by the elimination of 232 authorized non-permanent positions dedicated to risk management and compliance supervision and significant reductions in the budgets for Outside Services-Personnel (down $15.6 million, or 5.2 percent) and Equipment (down $15.8 million, or 17.3 percent). Most of the proposed reductions in Outside Services-Personnel and Equipment will occur in the Division of Information Technology (DIT) and CIO Council budgets. The Outside Services-Personnel reductions are primarily attributable to lower 2013 contracting requirements for IT infrastructure services and CIO Council system development projects. The Equipment reductions in the proposed 2013 budget reflect the elimination of one-time equipment and software costs that were budgeted in 2012 for the relocation of the FDIC's back-up data center and the payment of software licensing fees that were determined to be owed to certain vendors following a reconciliation of licensing fees paid for prior years. The ongoing operations component of the budget also includes $25 million in an unassigned contingency reserve (1.4 percent of the proposed 2013 ongoing operations budget),[6] to be administered by the CFO to provide funding for unanticipated operational requirements that emerge during the year, including the continuing refinement of staffing and other resource requirements to carry out the FDIC's new responsibilities for the resolution of SIFIs under DFA.

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[5]The value of the assets covered by the loss share agreements has fallen from approximately $135 billion at the beginning of the year to $110.6 billion (book value) on October 31.

[6]The Board approved an initial contingency reserve of $24 million in the 2012 ongoing operations budget.

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 2013, although this will be partially offset by increased post-failure receivership management workload. The Corporation will need fewer temporary employees and contractors in DRR and its supporting organizations and closed its temporary Midwest Satellite Office (MWSO) in September 2012. The proposed reductions are 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 spikes in workload. The proposed receivership funding budget for Outside Services-Personnel is $592,500,105, down $442,600,911 (42.8 percent) from 2012. The proposed 2013 receivership funding budget is also down significantly from 2012 levels in the Salaries and Compensation, Travel, Buildings and Leased Space, Equipment, and Other expense categories.

To ensure that the FDIC has the flexibility to respond quickly to unexpected changes in workload, the receivership funding budget component includes an unassigned contingency reserve of $12,631,949 (1.4 percent of the proposed receivership funding budget), to be administered by the CFO to ensure that the Corporation is prepared to respond quickly to any unexpected increase in failures or related workload that might arise during the year.

The FDIC cannot, of course, control the variable workload associated with the receivership funding component of the annual corporate operating budget, nor can it project with certainty the specific number and type of failures that will occur in 2013 or the actual expenses that will be incurred in connection with those failures. The proposed 2013 receivership funding budget may not, therefore, prove to be a reliable estimate of 2013 expenses for this budget component. Based upon what is known today, however, the proposed receivership funding budget will be sufficient to cover 2013 resolutions and receivership management expenses. The Board will be asked to approve additional funding if it is determined during the year that increased budget authority is needed for this component.

Overview of Proposed 2013 Budget by Major Expense Category

Attachment 1 itemizes the proposed 2013 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 2013 Salaries and Compensation budget is $1,373,214,041, which is $21,819,260 (about 1.6 percent) lower than the 2012 Salaries and Compensation budget. This is attributable largely to the fact that the Corporation is reducing the size of its receivership workforce. The proposed 2013 budget includes funding for approximately 616 fewer full-time equivalent employees than are included in the current 2012 budget. The Salaries and Compensation expense category represents 66.4 percent of the proposed 2013 ongoing operations budget, 21.0 percent of the proposed 2013 receivership funding budget, and 51.2 percent of the overall proposed 2013 Corporate Operating Budget.

- The proposed 2013 Outside Services-Personnel budget (for contractor-provided services) is $879,358,063, which is $488,231,203 (34.3 percent) lower than the 2012 budget. This decrease reflects primarily an expected reduction in insured institution failures in 2013 and a resulting decrease in the contractor support required to resolve failed institutions. The Outside Services-Personnel expense category represents about 16.1 percent of the proposed 2013 ongoing operations budget, 65.8 percent of the proposed 2013 receivership funding budget, and 32.8 percent of the overall proposed 2013 Corporate Operating Budget.

The remainder of the proposed 2013 Corporate Operating Budget consists of $131,265,699 for Travel expenses, down $14,114,819 (9.7 percent) from 2012, largely as a result of lower projected failure resolution activities; $129,417,587 for Buildings and Leased Space expenses, down $55,503,157 (30.0 percent) from 2012, driven by lower leased space requirements at the site of failures; $86,454,387 for Equipment expenses, down $17,884,331 (17.1 percent) from 2012, largely as a result of savings from non-recurring data center relocation and software licensing costs incurred during 2012; $24,221,173 for Outside Services-Other expenses, down $5,394,793 (18.2 percent) from 2012, primarily due to decreased receivership management activity; and $58,707,784 for Other Expenses, down $25,192,348 (30.0 percent) from 2012, primarily due to reduced receivership management activity.

2013 Staffing Authorizations

Overview of Proposed Changes in Authorized 2013 Staffing

The proposed 2013 Corporate Operating Budget includes a total authorized staffing level of 8,026 positions (5,833 permanent, 2,193 non-permanent), as shown in Attachment 6. This represents a net decrease of 678 positions from the authorized staffing level initially approved by the Board for 2012 and a net decrease of 687 positions from the current 2012 authorized staffing level. If approved by the Board, authorized permanent staffing would decrease in 2013 by two positions, while authorized non-permanent staffing would decline by 685 positions from current 2012 authorized staffing levels.

The largest permanent staffing increases are proposed in RMS (22 positions) and the Legal Division (18 positions). In addition, increases in authorized permanent staffing are proposed for DCP (6 positions), DIT (5 positions), and Corporate University (1 position). These permanent increases are offset by proposed permanent staffing reductions in DRR (24 positions), the OIG (14 positions), Corporate University's Corporate Employee Program (6 positions), the Division of Finance (5 positions), the Executive Offices (3 positions) and the Office of Minority and Women Inclusion (2 positions).

An increase in authorized non-permanent staffing is proposed for DIT (14 positions) in conjunction with a temporary need for more skilled IT project managers for the large number of major system modernization projects planned over the next several years. This increase is more than offset by proposed reductions in authorized non-permanent staffing in DRR (369 positions), RMS (177 positions), DCP (55 positions), DOA (47 positions), and the Legal Division (39 positions). Most of these non-permanent reductions are associated with continuing reductions in staffing needed to manage bank failure activities and the continuing decline in the number of troubled and problem institutions subject to FDIC supervision.

Staffing Flexibility

For the past two years, in conjunction with its approval of the annual corporate operating budget (including staffing authorizations), the Board has provided divisions and offices 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 delegation of authority are as follows:

- Each division and office may 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]

- The CFO may approve a division or office request for a cap higher than 2 percent if that organization is fully staffed up to the 2 percent limit and can demonstrate to the CFO, using objective quantitative data and analysis, that its attrition is likely to exceed 2 percent during the coming year because of projected retirements[8] 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" authorizations, that organization's "over-hire" authority is temporarily "grandfathered" at the higher level, and it may temporarily exceed the 2 percent limit until its excess permanent staffing drops 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 the Board continues this delegation of authority in 2013, it will permit the corporate-wide "over-hiring" of up to 78 permanent employees nationwide above authorized 2013 permanent staffing levels (absent approval by the CFO of higher limits in certain organizations).

Projected 2013 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 provides funding on a multi-year basis for major investment projects (mostly IT systems development projects) that are individually approved by the Board. Funds may not be reallocated among projects, and budget authority for a project expires when it is completed. The Capital Investment Review Committee

[7]For RMS and DCP, this authority is based on their permanent, non-examiner staffing authorization, excluding all authorized permanent non-supervisory field examination positions.
[8]Requests based on retirement projections are required to utilize the projections in the Division of Finance's annual *FDIC Retirement Analysis*.

(CIRC) monitors the progress of most approved investment projects and reports on them quarterly to the Board.

The Investment Budget currently includes three active investment projects; the Examination Tools Suite project, the Claims Administration System project, and the 550 HVAC Retrofit project. Investment Budget spending has declined from a high of $108 million in 2004 (when there were 10 approved investment projects underway) to $10 million spent during the first 10 months of 2012.

Overview of Attached Exhibits

Attachment 1 displays the proposed 2013 Corporate Operating Budget by major expense category. Attachment 2 displays the proposed 2013 Corporate Operating Budget by division and office. Attachments 3 and 4 display the proposed budget by division and 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 funding source. Attachment 6 shows proposed 2013 staffing authorizations (permanent and non-permanent) for each division and office. Also attached is the proposed 2013 Budget Resolution reflecting the recommendations outlined above.

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