Office of Inspector General

Office of Audits and Evaluations
Report No. AUD-14-001

The FDIC's Progress in Implementing Systemic Resolution Authorities under the Dodd-Frank Act

November 2013

Office of Inspector General

Executive Summary

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Why We Did the Audit

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) created a comprehensive new regulatory and resolution framework designed to avoid the severe consequences of financial instability. Among other things, the Dodd-Frank Act gave the FDIC broad new authorities to mitigate the risk of systemically important financial institutions (SIFIs) to the financial stability of the United States and, if necessary, to effect an orderly liquidation. The ability to mitigate risk and resolve SIFIs is critical to fulfilling the FDIC's primary mission of upholding public confidence in the nation's financial system. For that reason, the FDIC Chairman requested that the FDIC Office of Inspector General (OIG) review the Corporation's progress in implementing its systemic resolution authorities under the Dodd-Frank Act. The objective of this performance audit was to determine the progress made by the FDIC in implementing the Dodd-Frank Act authorities associated with monitoring SIFIs, and resolving one, should that be necessary.

Background

Title I of the Dodd-Frank Act provides tools for regulators to impose enhanced supervision and prudential standards on SIFIs. Title II of the Dodd-Frank Act includes a new orderly liquidation authority that can be invoked when the liquidation of a financial company under the Bankruptcy Code or other applicable law would have serious adverse effects on financial stability in the United States. In August 2010, the FDIC's Board of Directors (FDIC Board) established the Office of Complex Financial Institutions (OCFI) to serve as the focal point for implementing the Corporation's systemic resolution authorities. The FDIC Board intended for OCFI to coordinate with other FDIC divisions and offices for critical expertise and support in certain functional areas to implement the Corporation's systemic resolution authorities.

Overall Results and Recommendations

The FDIC has made significant progress over the past 3 years towards implementing its systemic resolution authorities under the Dodd-Frank Act. Among other things, the FDIC has:

- issued a joint regulation and met established timeframes for completing reviews of resolution plans submitted by covered financial companies,
- entered into agreements with certain foreign regulatory authorities to promote cross-border cooperation, and
- developed a single-point-of-entry resolution strategy as a preferred approach for the orderly liquidation of covered financial companies under certain circumstances.

While these accomplishments are notable, more work remains to be done to establish a robust corporate-wide capability for this critical responsibility. In this regard, we are making six recommendations to the FDIC Chairman that are intended to better position the FDIC to face future challenges and successfully carry out its systemic resolution authorities under the Dodd-Frank Act. In general, the recommendations are aimed at enhancing the FDIC's long-term strategic planning efforts, strengthening coordination among FDIC divisions, and building out OCFI's infrastructure to support systemic resolution activities.

Corporation Comments

The FDIC Chairman provided a written response, dated November 6, 2013, to a draft of the report. In the response, the FDIC Chairman concurred with all six of the report's recommendations and described ongoing and planned actions that address the recommendations. We will continue to monitor the FDIC's progress in fully implementing these actions and will re-evaluate the Corporation's readiness, as warranted.

Federal Deposit Insurance Corporation
3501 Fairfax Drive, Arlington, VA 22226 Office of Inspector General

DATE: November 14, 2013

MEMORANDUM TO: Martin J. Gruenberg
Chairman

/Signed/
FROM: Fred W. Gibson, Jr.
Acting Inspector General

SUBJECT: *The FDIC's Progress in Implementing Systemic Resolution Authorities under the Dodd-Frank Act* (Report No. AUD-14-001)

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) gave the FDIC broad new authorities to mitigate the risk of systemically important financial institutions (SIFIs) to the financial stability of the United States and, if necessary, to effect an orderly liquidation. The ability to mitigate risk and resolve SIFIs is a significant expansion of the FDIC's mission, and this audit responds to your request that the Office of Inspector General review the FDIC's progress in that area.

As discussed in the report, we found that the FDIC has made significant progress over the past 3 years towards implementing its systemic resolution authorities under the Dodd-Frank Act. Among other things, the FDIC has issued a joint regulation and met established timeframes for the review of resolution plans, entered into agreements with certain foreign regulatory authorities to promote cross-border cooperation, and developed a preferred resolution strategy for the orderly liquidation of covered financial companies under certain circumstances.

While these accomplishments are notable, more work remains to be done to establish a robust corporate-wide capability for this critical responsibility. In this regard, we made six recommendations that are intended to better position the FDIC to face future challenges and successfully carry out its systemic resolution responsibilities under the Dodd-Frank Act. The ongoing and planned actions described in your response to our report are responsive to the recommendations. We will continue to monitor the Corporation's progress in fully implementing these actions and will re-evaluate the Corporation's progress in carrying out its new resolution authorities, as warranted.

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Why We Conducted the Audit

- The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) provided the FDIC with broad new authorities to prevent or mitigate the risk of systemically important financial institutions* (SIFIs) to the financial stability of the United States (U.S.) and, if necessary, effect an orderly liquidation.

- The ability to implement those authorities, if needed, is critical to fulfilling the FDIC's primary mission of upholding public confidence in the nation's financial system.

- For these reasons, the FDIC Chairman requested that the Office of Inspector General (OIG) review the Corporation's progress in implementing its systemic resolution authorities under the Dodd-Frank Act.

* Terms that are dash underlined when first used in this report are defined in Appendix 3, *Glossary of Terms.*

Audit Objective and Approach

- The objective of this performance audit was to determine the progress made by the FDIC in implementing the Dodd-Frank Act authorities associated with monitoring SIFIs, and resolving one, should that be necessary. To achieve our objective, we:
  - identified key provisions of the Dodd-Frank Act pertaining to systemic resolutions and assessed the extent to which the FDIC implemented the provisions, and
  - assessed the status of the organizational development (i.e., infrastructure) of the Office of Complex Financial Institutions (OCFI)—the FDIC's office with primary responsibility for implementing systemic resolution authorities.
- Although we mention some of the early challenges faced by OCFI, our audit focused on current progress and conditions, and our recommendations are designed to further the FDIC's ongoing efforts to carry out its systemic resolution authorities under the Dodd-Frank Act.
- Key criteria used during the audit include the Dodd-Frank Act, reports and publications issued by the Government Accountability Office (GAO) on internal controls and mergers, and industry studies on management challenges with new organizations.
- Appendix 1 more fully describes our objective, scope, and methodology.

Background–
New Systemic Resolution Authorities

The enactment of the Dodd-Frank Act in July 2010 substantially changed the FDIC's mission by giving the Corporation broad new authorities to mitigate the risk of SIFIs to the stability of the U.S. financial system and, if necessary, effect an orderly liquidation of such institutions. The FDIC's systemic resolution authorities fall within Titles I and II of the Dodd-Frank Act.

Title I
Resolution Plan Review – The FDIC is required to review, in conjunction with the Board of Governors of the Federal Reserve System (the Federal Reserve), resolution plans or "living wills" (hereinafter referred to as 165(d) Plans) submitted by covered financial companies. If the FDIC and the Federal Reserve jointly determine that a plan is not credible or would not facilitate an orderly resolution of the company under the Bankruptcy Code, then they must notify the company of the deficiencies in the plan.
Back-up Examination and Enforcement – The FDIC received additional back-up examination authority, under certain circumstances, for nonbank financial companies and large bank holding companies. The FDIC also now has authority to initiate enforcement actions against bank holding companies.

Title II
Initiate Orderly Liquidation – The FDIC can take steps to initiate an orderly liquidation of a covered financial company through its participation in a recommendation to the Secretary of the Department of the Treasury (the Treasury) to appoint the FDIC as receiver based on eight criteria, as described in Appendix 2. Initiation requires action by three parties (known as the three keys): the Federal Reserve; the Secretary of the Treasury; and (depending on the nature of the covered financial company) either the FDIC, the Securities and Exchange Commission (SEC), or the Federal Insurance Office (FIO).
Execute Orderly Liquidation – The FDIC has been given the authority to liquidate failing financial companies; appoint the Securities Investor Protection Corporation (SIPC) as trustee for a covered broker dealer; and, if necessary, stand in the place of a state regulator to place an insurance company in liquidation.

Background–
The Creation of OCFI

The FDIC was proactive in preparing for its new systemic resolution authorities and established a new office to lead the implementation of these activities.

- In 2009, the FDIC Chairman established a Strategic Resolution Authority Project to formulate an organizational strategy and began work on an implementation plan. That project was superseded by the Systemic Resolutions Steering Committee, which was a multi-divisional effort to recommend an organizational strategy for addressing the FDIC's new systemic resolution authorities.

- In August 2010, based on the Systemic Resolutions Steering Committee's recommendation, the FDIC's Board of Directors (FDIC Board) established OCFI to serve as the focal point for implementing the systemic resolution authorities. OCFI's three core functions were:

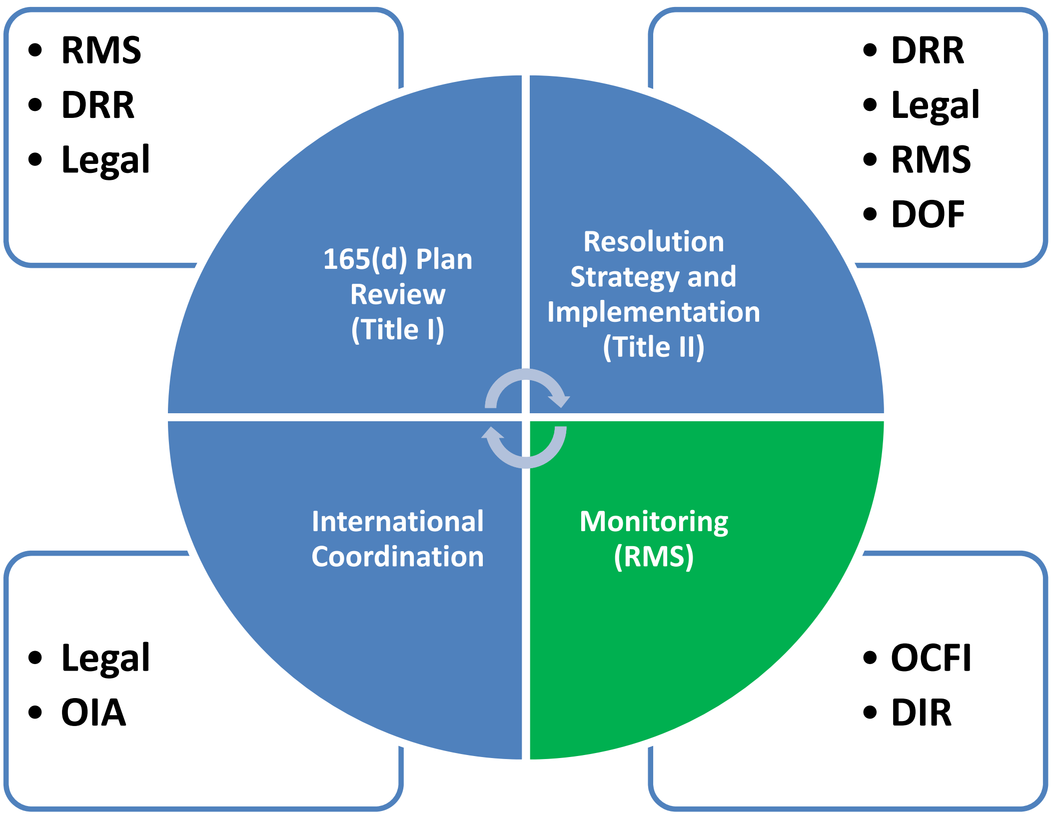
    1. **Monitoring**—Responsible for monitoring risk within and across large, complex financial companies for back-up supervisory and resolution readiness purposes. Monitoring was transferred from OCFI to the FDIC's Division of Risk Management Supervision (RMS) in March 2013**.**

    2. **Systemic Resolution Planning and Implementation**—Responsible for reviewing 165(d) Plans (as well as certain resolution plans submitted by insured depository institutions pursuant to a rule issued under the Federal Deposit Insurance Act).

    3. **International Coordination**—Responsible for coordinating with regulators overseas regarding challenges with cross-border resolutions.

Background–Interaction of OCFI and Other Corporate Stakeholders

The FDIC Board intended for OCFI to utilize other FDIC divisions and offices for critical expertise and support in certain functional areas to implement the Corporation's systemic resolution authorities.



RMS, the Legal Division (Legal) , Division of Resolutions and Receiverships (DRR), Division of Finance (DOF), Office of International Affairs (OIA), and Division of Insurance and Research (DIR) have expertise in their respective areas to enhance OCFI's resolution efforts.

The Divisions of Administration and Information Technology also provide resource management services that support the FDIC's systemic resolution efforts.

Overall Results

The FDIC has made significant progress over the past 3 years towards implementing its systemic resolution authorities under the Dodd-Frank Act. Among other things, the FDIC has:

- issued a joint regulation and met established timeframes for completing reviews of 165(d) Plans submitted by covered financial companies,
- entered into agreements with certain foreign regulatory authorities to promote cross-border cooperation, and
- developed a single-point-of-entry resolution strategy as a preferred approach for the orderly liquidation of covered financial companies under certain circumstances.

While these accomplishments are notable, more work remains to be done to establish a robust corporate-wide capability for this critical responsibility. As described later, OCFI needed to fully involve and consider the related roles and complementary functions that other FDIC divisions have in implementing the FDIC's systemic resolution authorities. In that regard, FDIC management began to take steps in the fall of 2012 to promote a more corporate focus in OCFI's approach to systemic resolutions. OCFI can further these ongoing efforts by:

- engaging key corporate stakeholders to fully define the logistics, roles and responsibilities, preparation activities, and resources needed to execute resolution strategies, including the single-point-of-entry.
- enhancing its strategic plan for implementing the FDIC's systemic resolution authorities to more clearly link ongoing and planned projects and existing performance measures to long-term goals and priorities and more effectively measure progress toward readiness.

Overall Results

In addition, the FDIC would benefit from continuing to formalize coordination between OCFI and RMS for Monitoring; evaluating whether current staffing levels and skill sets are sufficient to address systemic resolution authorities; enhancing protocols for discovering, obtaining, and sharing information for SIFIs across the FDIC; and strengthening policies and procedures for key processes, where appropriate.

Given the potentially volatile nature of global economic conditions and the ever-present risks of SIFIs, we recommend that the FDIC Chairman ensure that priority attention is given to the aforementioned activities. Doing so will better position the FDIC to face future challenges and successfully carry out its systemic resolution authorities under the Dodd-Frank Act.

Implementation of Systemic Resolution Authorities–Progress

The FDIC has made significant progress in implementing its systemic resolution authorities for institutions where the scale and complexity of the institutions, in terms of operations and global reach, is far greater than the financial institutions that have been supervised and resolved in the past.

1. <u>165(d) Plan Reviews</u>
   - Issued a joint regulation and guidance with the Federal Reserve concerning the review of 165(d) Plans.
   - Met regulatory deadlines for information completeness reviews for the first group of financial company filers.

2. <u>Expanded Back-up Examination Authority and Enforcement Authority</u>
   - Participated in capital and liquidity projects with the Federal Reserve.
   - Continued on-site placement of FDIC examiners at U.S.-based SIFIs.

3. <u>Initiate Orderly Liquidation</u>
   - Conducted several table top simulations and facilitated planning discussions for resolving a SIFI.

Implementation of Systemic Resolution Authorities–Progress

4. <u>Execute Orderly Liquidation</u>

   - Developed a single-point-of-entry resolution strategy as the preferred approach for the orderly liquidation of a covered financial company under certain circumstances. The strategy was well received by the financial markets and global regulators. The FDIC plans to seek public comment on this strategy by the end of 2013.
   - Developed draft internal resolution plans for U.S.-based SIFIs that assess an institution's size and scope, leverage and liquidity, interconnection with other companies, complexity, substitutability, and other issues in considering whether traditional bankruptcy is feasible and mitigating activities are applicable or whether a Title II orderly liquidation may be necessary.
   - Identified the jurisdictions where important functions and critical operations of SIFIs are located.
   - Executed agreements on the exchange of information and cooperation in resolving troubled cross-border financial institutions with certain foreign regulatory authorities based upon the jurisdictions where important functions and critical operations of SIFIs are located. Discussions are underway to establish similar agreements with other foreign regulatory authorities.

Implementation of Systemic Resolution Authorities–Title II Execution

OCFI needs to engage key corporate stakeholders to more fully define the logistics, roles and responsibilities, preparation activities, and resources needed to carry out systemic resolution strategies, including the single-point-of-entry.

- More work remains to achieve a robust corporate-wide operational capability to execute resolution strategies, including the single-point-of-entry. Such capabilities must remain flexible and scalable to address various resolution scenarios, the specific needs and legal structure of the financial companies involved, and current facts and circumstances (e.g., prevailing market conditions and potential impact on counterparties).

- The execution of any resolution strategy, including the single-point-of-entry strategy, will require a corporate-wide response, and OCFI must fully consider the impact that the strategy's execution could have on the Corporation. In that regard, OCFI must engage other FDIC divisions and offices, such as DRR and RMS, in preparation efforts.

- By defining and coordinating such preparation requirements across the FDIC, and establishing goals and timelines for those efforts, the FDIC can better measure progress towards its readiness to execute resolution strategies.

Implementation of Systemic Resolution Authorities–Project Management

OCFI initially implemented the FDIC's systemic resolution authorities on a project-by-project basis. Going forward, OCFI would benefit from enhancing its strategic plan to clearly demonstrate how ongoing and planned projects and existing performance measures support long-term goals and priorities. Such a plan would further facilitate measuring progress towards operational readiness.

- The best practices of successful organizations suggest that management develop an organization's mission and strategic goals to support that mission, establish implementation goals and timelines, and link projects to specific implementation goals. Projects are the building blocks for achieving strategic goals. Such an approach can pinpoint performance shortfalls and gaps and identify needed corrections.

- OCFI initiated projects as a means of testing strategies for addressing systemic resolution authorities. These projects were generally developed autonomously by, and managed within, OCFI's functional groups and were the drivers for the deployment of OCFI resources.

- OCFI should continue to improve its internal coordination across projects to strengthen performance, and ensure that project priorities are clearly defined and linked with long-term strategic goals.

Implementation of Systemic Resolution Authorities–The Role of Monitoring

In March 2013, FDIC management transferred the staff and functions of Monitoring from OCFI to RMS after concluding that it would be more effective and efficient to use RMS' existing infrastructure for this activity. OCFI and RMS should continue to build out and formalize coordination for Monitoring activities.

- The best practices of successful organizations indicate that when staff from one organization must support another organization, roles and responsibilities must be clearly established.

- Monitoring was established within OCFI to assess risk within and across large, complex financial companies for back-up supervisory and resolution readiness purposes. The institutional knowledge and analysis associated with Monitoring are relevant to OCFI's 165(d) Plan reviews, orderly liquidation, and international functions. More work remains to be done to increase collaboration across OCFI and RMS to further integrate these functions going forward.

- The roles and responsibilities of Monitoring staff must be clearly defined, understood, and managed to ensure the effective coordination and exchange of risk analyses and other information and to mitigate the risk of conflicts in priorities and direction, and ultimately, inefficiencies.

Implementation of Systemic Resolution Authorities–FDIC Changes

The FDIC has established a number of internal governing bodies and processes that play a role in implementing key aspects of the FDIC's systemic resolution authorities. These include, but are not limited to, the following:

- OCFI Resolution Plan Review Committee. Established by the OCFI Director in June 2012, the Committee is responsible for reviewing, considering, and making recommendations to the FDIC Board and Chairman's office regarding resolution plans submitted by covered financial companies and certain insured depository institutions that are assigned to OCFI for oversight and resolution planning. The Committee also reviews Title II resolution plans prepared by OCFI prior to their presentation to the FDIC Board or other outside entities.

- Executive Management Committee (EMC). Established by the Chairman in July 2012, the Committee is responsible for assisting the FDIC Board and Chairman in the day-to-day operational and strategic management of the agency. In late 2012, the Chairman asked the EMC to coordinate with other senior FDIC executives to provide increased oversight of OCFI's operations, particularly in the area of Monitoring. In connection with this oversight, several executive managers were detailed to work in OCFI.

Implementation of Systemic Resolution Authorities–FDIC Changes

- Supervisory Risk and Resolutions Activities Plans. Created in February 2013 by OCFI, the plans are intended to serve as an annual planning document for the FDIC's supervisory and resolution planning activities related to each SIFI. These plans are developed on a collaborative basis by representatives in OCFI, RMS, and Legal.

- SIFI Cross-Discipline Information Exchange. Created in March 2013, this exchange provides a forum for FDIC staff with knowledge of SIFIs to discuss issues and plan FDIC activities.

- EMC-Complex Financial Institution Coordination Group (EMC-CFI). Established in May 2013 by the EMC, the group facilitates communication, coordination, consistency, and agreement throughout the FDIC regarding CFI-related activities and reviews, and concurs in recommendations and actions on CFI-related matters prior to submission to the FDIC Board. The EMC-CFI, which includes senior executives from several FDIC divisions, also addresses readiness measurement and coordination.

OCFI Organizational Development–Overview

As a new organization, OCFI was presented with the challenge of implementing significant new resolution authorities while simultaneously building out an infrastructure to support its mission.

- Our research of best practices indicates that new organizations are more likely to be successful when they effectively:
  - balance achieving new strategic objectives with organizational development activities,
  - establish an organization-wide knowledge and skills inventory to exchange knowledge among functional groups and other divisions, and
  - attract and retain talent.
- OCFI faced several challenges related to its organizational development, such as:
  - determining and maintaining an appropriate level of staffing and skill sets commensurate with the FDIC's new resolution authorities,
  - implementing protocols for the efficient collection and sharing of information, and
  - developing policies and procedures.

OCFI Organizational Development–Staffing and Skill Sets

New statutory authorities and stringent regulatory deadlines resulted in the FDIC rapidly hiring staff into a newly created organization that lacked a solid infrastructure. This condition resulted in some initial skills and expectation mismatches that contributed to staff turnover.

- OCFI's initial staffing and skill sets were determined before the level of effort associated with key authorities was fully understood. The unique nature of OCFI's new responsibilities—compared to other FDIC divisions with long-standing and well-defined missions—made estimating required staffing levels and skill sets difficult.

- During 2011, OCFI brought a significant number of staff on board. Contributing to this rapid hiring was a 2011 Corporate Performance Objective that focused on quickly filling vacant OCFI positions. In addition, OCFI placed heavily reliance on employee details from other FDIC divisions and offices to meet its responsibilities during 2011 and 2012.

- The FDIC's decision to rapidly hire and detail personnel to OCFI before operational strategies and senior management were in place to integrate and lead new staff contributed to an environment of continual change and contributed to OCFI experiencing an overall employee turnover rate of 20 percent in 2012.

- As OCFI has worked to better define its responsibilities and processes, OCFI management recognizes that its staffing levels may need to be adjusted and that additional specialized expertise may be needed in some areas.

OCFI Organizational Development– Information

OCFI had not established sufficient protocols to discover, obtain, and share business information within and outside of the FDIC.

- OCFI requires comprehensive, accurate, and timely information to monitor and ensure readiness to effectively resolve SIFIs. That information must be aggregated and analyzed to plan, develop, and implement strategies that minimize the overall cost of resolutions and mitigate systemic risk.

- Initially, each OCFI functional group managed its own information without an effective mechanism to exchange or discover information located within OCFI or other FDIC divisions. Additionally, OCFI requests for information from other regulators were not always coordinated within OCFI. Without clear information protocols in these areas, OCFI experienced inefficiencies in obtaining information from internal and external sources.

- OCFI invested approximately $6.2 million in two information systems without fully assessing its long-term information needs. As a result, these information systems did not meet their intended objectives. OCFI discontinued new funding for the two information systems when it became apparent that they were not effectively supporting OCFI's business operations.

- As described later, OCFI prepared an IT Plan during our audit and presented it to the FDIC's Chief Information Officer (CIO) Council for review and discussion. This plan is an important step towards strengthening protocols for discovering, obtaining, and sharing information.

OCFI Organizational Development– Policies and Procedures

Although OCFI developed resolution strategies and established policies and procedures in some areas, formal policies and procedures are not yet in place for all key processes. Written policies and procedures are an important control for ensuring that processes are repeatable, consistent, and disciplined and for reducing operational risk associated with staff turnover.

Much of OCFI's attention during its first years of operation focused on formulating strategies to address the FDIC's systemic resolution authorities. Now that such strategies are generally in place, priority attention should be placed on documenting policies and procedures. The table below summarizes the status of policies and procedures for key Title I and Title II processes.

OCFI Process	Status of Policies and Procedures
165(d) Plan Review	OCFI finalized the OCFI Resolution Plan Review Manual –2013 in March 2013. This manual was updated in June 2013 and, according to OCFI officials, is reviewed quarterly and updated as necessary.
Back-up Examination and Enforcement	The FDIC has drafted a list of key processes for the additional back-up examination authority it received under the Dodd-Frank Act for nonbank financial companies and large bank holding companies. The FDIC has also outlined the flow of monitoring activities within and across these institutions. During our audit, Monitoring moved to RMS and significant changes were being made to its processes. Monitoring is in the process of drafting policies and procedures.
Initiate Orderly Liquidation	An FDIC Board case template has been developed to recommend an orderly liquidation, if it becomes necessary to do so. An interagency working group is developing the metrics and processes to support a formal recommendation for an orderly liquidation.
Execute Orderly Liquidation	Title II resolution strategies have been developed for specific SIFIs. A draft Title II Procedure Manual has also been developed. In addition, agreements have been executed with countries where a systemic resolution would have the greatest potential impact, and efforts to execute agreements with other countries are ongoing.

OCFI Organizational Development– FDIC Changes

OCFI has taken, and continues to take, steps to address issues associated with its staffing and skill sets, protocols for collecting and sharing information, and policies and procedures.

- Staffing and Skill Sets
  - OCFI is aware that additional specialized expertise may be needed in some areas and is contemplating the appropriate mix of skill sets to accomplish its mission. In addition, OCFI plans to place greater emphasis on developing important skill sets through training.
  - OCFI is working to develop formal protocols with other FDIC divisions to ensure staff resources are shared and leveraged appropriately.
- Information Technology
  - OCFI has formed internal governance bodies to oversee its IT initiatives. These groups will inform OCFI's representative to the FDIC's CIO Council of the bodies' interactions, as well as communications with other inter-divisional groups.

OCFI Organizational Development–FDIC Changes

- Information Technology (continued)
  - In response to concerns raised by the FDIC's CIO Council in the fall of 2012, OCFI developed a high-level IT Plan and provided it to the CIO Council in March 2013. The plan emphasized the need to collaborate with other business line divisions and DIT to:
    - leverage previous IT investments and existing information and technology,
    - make adjustments based on 2012 experiences,
    - improve the organization of unstructured and structured information to assist in discovery and access, and
    - obtain and organize high-priority structured data that is not available within the FDIC datacenter.
  - OCFI will also undertake a strategic planning project to identify a 3-5 year maturation of current information and technology it needs to accomplish its mission.
- Policies and Procedures
  - OCFI was working to update and refine written policies and procedures for a number of its processes.
    - Monitoring was working to develop and issue a Risk Assessment Manual that defines the framework for conducting monitoring, risk assessments, and back-up examination activities.
    - An interagency working group is developing metrics and processes for supporting formal recommendations for orderly liquidation.

OCFI Organizational Development– FDIC Changes

- OCFI has established a number of priority initiatives as part of the FDIC's 2013 Performance Goals that are intended to address issues with staffing and skill sets, management systems, internal controls, and policies and procedures. OCFI reports to senior FDIC management on its progress in addressing these priority initiatives on a quarterly basis.

- The OCFI 2013 Strategic Plan includes target dates for completing policies and procedures related to Title I and Title II as well as a framework for monitoring, risk assessment, and back-up examination activities.

Recommendations

The FDIC has taken a number of steps to address the issues we identified pertaining to the implementation of systemic resolution authorities and OCFI's infrastructure. To further the FDIC's ongoing efforts in this area, we recommend that the FDIC Chairman ensure that priority attention is given to the activities listed below. The EMC-CFI Group, which was established to promote coordination and communication regarding systemic resolution issues throughout the FDIC, may be an advantageous means to monitor these activities.

1. Fully define and build consensus among corporate stakeholders regarding the logistics, roles and responsibilities, preparation activities, and resource allocation in both OCFI and other divisions and offices necessary to execute resolution strategies.

2. Enhance OCFI's strategic plan for implementing the FDIC's systemic resolution authorities by:
   - Ensuring ongoing and planned projects and existing performance measures are integrated and linked to long-term goals and priorities, and
   - Including aggressive, but achievable, milestones for measuring progress towards readiness and a mature OCFI organization.

3. Continue to build out and formalize coordination between OCFI and RMS regarding the Monitoring function.

Recommendations

4. Evaluate the sufficiency of staffing levels and skill sets for OCFI and other FDIC divisions and offices with resolution responsibilities—taking into consideration prior staff turnover—and determine a course of action for addressing identified gaps.

5. Strengthen and formalize protocols to ensure OCFI staff can efficiently discover, obtain, and share internal and external information.

6. Establish timeframes and assign necessary resources for developing policies and procedures as soon as practical for key processes associated with the implementation of systemic resolution authorities.

We will continue to monitor the FDIC's progress in fully implementing these activities and will re-evaluate its readiness, as warranted.

Corporation Comments and OIG Evaluation

The FDIC Chairman provided a written response, dated November 6, 2013, to a draft of this report. The response is presented in its entirety in Appendix 5. In the response, the Chairman concurred with all six of the report's recommendations and described completed and planned corrective actions that address the recommendations.

A summary of the Corporation's corrective actions is presented in Appendix 6. The completed or planned actions are responsive to the recommendations, and the recommendations are resolved.

Appendix 1: Objective, Scope, and Methodology

Audit Objective

- The objective of the performance audit was to determine the progress made by the FDIC in implementing the Dodd-Frank Act authorities associated with monitoring SIFIs, and resolving one, should that be necessary.

- We conducted the audit from March 2013 through July 2013 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Scope and Methodology

- The scope of the audit included assessing the FDIC’s progress in implementing its Dodd-Frank Act authorities pertaining to systemic resolutions through July 2013. Although our work included gaining an understanding of the operational challenges that OCFI experienced following its creation, the focus of our work was on the steps that FDIC management was taking to address those issues and the Corporation’s key accomplishments, progress, and challenges.

Appendix 1: Objective, Scope, and Methodology

- To accomplish our objective, we:
  - Reviewed the provisions of the Dodd-Frank Act pertaining to systemic resolutions and identified what we determined to be the FDIC's key authorities in this area.
  - Assessed the FDIC's progress in implementing the key authorities by identifying the primary processes and controls that the FDIC had established (or was working to establish) to address the authorities. We identified these processes and gained an understanding of them by:
    - interviewing senior managers and staff in FDIC business divisions and offices with responsibility for implementing systemic resolution authorities, including OCFI, DRR, RMS, DIR, the Division of Consumer Protection, and Legal;
    - analyzing and reviewing relevant documentation, such as FDIC management's memorandum to the Board establishing OCFI; relevant policies, procedures, and guidance; internal FDIC correspondence; and speeches and Congressional testimony by FDIC officials; and
    - observing CIO Council meetings and reviewing IT planning documents.
  - Assessed the status of OCFI's organizational development, including staffing and skill sets, protocols for information gathering and analysis, and policies and procedures, using the following criteria:
    - GAO's November 1999 *Standards for Internal Control in the Federal Government*. This publication describes, among other things, the importance of human capital, IT, and policies and procedures;
    - The FDIC Board case establishing OCFI. The case describes the FDIC Board's intent to have OCFI provide strategic direction to the FDIC in implementing systemic resolution authorities;
    - The best practices described in GAO's July 2003 report, entitled *Implementation Steps to Assist Mergers and Organizational Transformations*. These best practices stress the importance of governance in developing strategic goals, an implementation team, and a communications strategy;

Appendix 1: Objective, Scope, and Methodology

- The lessons learned contained in the Partnership for Public Service's August 2011 report, entitled *Securing the Future Management Lessons of 9/11*. The report reflects the results of interviews of numerous leaders involved in the standup and operation of the Department of Homeland Security and Office of the Director of National Security. The report describes the management challenges involved in building these two government agencies and lessons that can be applied to restructuring efforts today and in the future; and
- The concepts in the Human Resources Planning study, entitled *Challenges and Strategies of Matrix Organizations: Top-Level and Mid-Level Managers' Perspectives*. The study describes the inherent risks associated with personnel who report to more than one division.

Internal Control, Reliance on Computer-processed Information, Performance Measurement, Compliance with Laws and Regulations, and Fraud and Abuse

- As described in the Scope and Methodology section of this appendix, we performed audit procedures to identify and obtain an understanding of the FDIC's processes for implementing its systemic resolution authorities under the Dodd-Frank Act. However, consistent with our audit objective, we did not assess the effectiveness of those processes. For example, we did not assess the adequacy of the FDIC's reviews of 165(d) Plans for informational completeness or the FDIC's monitoring of financial companies.

- We did not rely on automated information from the FDIC's information systems that were significant to our audit objective, conclusions, or findings. Accordingly, we did not assess the effectiveness of information system controls.

Appendix 1: Objective, Scope, and Methodology

- The Government Performance and Results Act of 1993 (the Results Act), as amended, directs Executive Branch agencies to develop a customer-focused strategic plan, align agency programs and activities with concrete missions and goals, and prepare and report on annual performance plans. As described in the report, we assessed strategic planning related to the FDIC's implementation of new Dodd-Frank Act authorities, including determining how FDIC division and office projects were integrated into long-term planning goals. We determined that the FDIC can further its strategic planning efforts by more clearly linking ongoing projects and existing performance measures to long-term goals and priorities. Such action would facilitate measuring progress toward readiness.

- Regarding compliance with laws and regulations, we assessed the FDIC's progress in implementing its systemic resolution authorities under the Dodd-Frank Act and related regulations, such as the Final Rule, entitled *Resolution Plans Required*, issued by the FDIC and FRB on November 1, 2011.

- We assessed the risk of fraud and abuse related to our audit objective in the course of evaluating audit evidence.

Appendix 2: Criteria for Initiating an Orderly Liquidation

- An FDIC Board case is prepared to determine whether to recommend to the Secretary of the Treasury that a covered financial company be placed into Orderly Liquidation under Title II of the Dodd-Frank Act. The Board case must include the following information regarding the covered financial company:
  - An evaluation of whether the financial company is in default or in danger of default.
  - A description of the effect that the default of the financial company would have on the financial stability of the United States.
  - A description of the effect that the default of the financial company would have on economic conditions or financial stability for low income, minority, or underserved communities.
  - A recommendation regarding the nature and the extent of actions to be taken under Title I of the Dodd-Frank Act regarding the financial company.
  - An evaluation of the likelihood of a private sector alternative to prevent the default of the financial company.
  - An evaluation of why a case under the Bankruptcy Code is not appropriate for the financial company.
  - An evaluation of the effects on creditors, counterparties, and shareholders of the financial company and other market participants.
  - An evaluation of whether the company satisfies the definition of a financial company under section 201 of the Dodd-Frank Act.

Appendix 3: Glossary of Terms

Term	Definition
Default or in Danger of Default	Defined in section 203(c)(4) of the Dodd-Frank Act (12 U.S.C. §5383) as a financial company considered to be in default or in danger of default if, (1) a case has been, or likely will promptly be, commenced with respect to the financial company under the Bankruptcy Code; (2) the financial company has incurred, or is likely to incur, losses that will deplete all or substantially all of its capital, and there is no reasonable prospect for the company to avoid such depletion; (3) the assets of the financial company are, or are likely to be, less than its obligations to creditors and others; or (4) the financial company is, or is likely to be, unable to pay its obligations (other than those subject to a bona fide dispute) in the normal course of business.
Nonbank Financial Company	The term "nonbank financial company" is defined in section 102(a)(4) of the Dodd-Frank Act (12 U.S.C. §5311) as either (1) a ''foreign nonbank financial company'' which is a company (other than a company that is, or is treated in the United States as, a bank holding company) that is incorporated or organized in a country other than the United States; and predominantly engaged in, including through a branch in the United States, financial activities; or (2) a "U.S. nonbank financial company" which is any U.S. company (other than a bank holding company, a Farm Credit System institution chartered and subject to the provisions of the Farm Credit Act of 1971 (12 U.S.C. 2001 et seq.), or a national securities exchange (or parent thereof), clearing agency (or parent thereof, unless the parent is a bank holding company), security-based swap execution facility, or security-based swap data repository registered with the Commission, or a board of trade designated as a contract market (or parent thereof), or a derivatives clearing organization (or parent thereof, unless the parent is a bank holding company), swap execution facility or a swap data repository registered with the Commodity Futures Trading Commission), that is (i) incorporated or organized under the laws of the United States or any State; and (ii) predominantly engaged in financial activities.
Resolution Plan	Defined in section 165(d) of the Dodd-Frank Act (12 U.S.C. §5365) as a plan required of each nonbank financial company supervised by the Board of Governors and certain bank holding companies describing activities for the company's rapid and orderly resolution in the event of material financial distress or failure. Title I Resolution Plans are also referred to as 165(d) plans or "living wills."

Appendix 3: Glossary of Terms

Term	Definition
Single-Point-of-Entry Resolution Strategy	The preferred resolution strategy of the FDIC to execute its orderly liquidation authority under Title II of the Dodd-Frank Act for systemically important financial companies. Under the approach, the FDIC will be appointed receiver of the top-tier parent holding company of the financial group following the company's failure and the completion of the appointment process set forth under the Dodd-Frank Act.
Systemically Important Financial Institution (SIFI)	The Dodd-Frank Act does not use the term "systemically important financial institution" (SIFI). This term is commonly used by academics and other experts to refer to bank holding companies with $50 billion or more in total consolidated assets and nonbank financial companies designated by the Financial Stability Oversight Council for Federal Reserve supervision and enhanced prudential standards of the Dodd-Frank Act (12 U.S.C. §§ 5322 and 5323).

Appendix 4: Acronyms and Abbreviations

Acronym/ Abbreviation	Explanation
CIO	Chief Information Officer
DIR	Division of Insurance and Research
DIT	Division of Information Technology
DRR	Division of Resolutions and Receiverships
EMC-CFI	Executive Management Committee – Complex Financial Institution Coordination Group
FIO	Federal Insurance Office
GAO	Government Accountability Office
IT	Information Technology
Legal	Legal Division
OCFI	Office of Complex Financial Institutions
OIA	Office of International Affairs
OIG	Office of Inspector General
RMS	Division of Risk Management Supervision
SEC	Securities and Exchange Commission
SIPC	Securities Investor Protection Corporation

Appendix 5: Corporation Comments

FDIC

Federal Deposit Insurance Corporation
550 17th Street NW, Washington, D.C. 20429 Office of the Chairman

DATE: November 6, 2013

MEMORANDUM TO: Fred W. Gibson
Acting Inspector General

FROM: Martin J. Gruenberg /**Signed**/
Chairman

SUBJECT: Response to Recommendations in the Audit Report Entitled, *The FDIC's Progress in Implementing the Systemic Resolution Authorities under the Dodd-Frank Wall Street Reform and Consumer Protection Act* (Assignment No. 2013-021)

This report was done in response to my request that the Office of Inspector General (OIG) review the FDIC's progress in implementing the systemic resolution authorities under the Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA). We concur with the audit results that confirm that the FDIC has made significant progress over the past three years in implementing the key elements of the DFA regarding the resolution of systemic entities. Among other things, the report notes that the FDIC has:

- promulgated a series of regulations implementing the new authorities under Title I and Title II of the DFA,
- met established timeframes for completing reviews of 165(d) Plans submitted by firms,
- issued guidance to the firms to detail what information should be included in their 2013 resolution plan submissions,
- been developing a resolution strategy to implement the Orderly Liquidation Authority, and
- entered into agreements with certain foreign regulatory authorities to promote cross-border cooperation.

The audit report makes six recommendations that are intended to better position the FDIC to continue the successful implementation of the DFA. The FDIC agrees with all of the recommendations in the audit report. The specific actions that the FDIC will undertake to address each of these recommendations are briefly described below.

OIG Audit Recommendation 1: *Fully define and build consensus among corporate stakeholders regarding the logistics, roles and responsibilities, preparation activities, and resource allocation in both OCFI and other divisions and offices necessary to execute resolution strategies.*

FDIC Response: The FDIC concurs with the recommendation. In May 2013, the FDIC created the Complex Financial Institution Coordination Group (CCG) to facilitate communication,

Appendix 5: Corporation Comments

coordination, consistency and agreement throughout the FDIC regarding activities related to complex financial institutions. The CCG operates under the Executive Management Committee (EMC) and provides general oversight and serves as an interdivisional communication and coordination clearinghouse on matters involving institutions with total assets greater than $10 billion. The CCG is responsible for reviewing recommendations and strategies on matters related to complex financial institutions and must concur on such recommendations and strategies prior to submission to the FDIC Board of Directors. The CCG serves as the forum for consensus building among stakeholders and creates accountability across the FDIC on important, cross-cutting operational and policy-related matters related to monitoring and resolution of complex financial institutions.

The CCG meets on a bi-weekly basis and additional meetings are added, as needed. In addition, on a quarterly basis, commencing on March 31, 2014, a special session of the CCG will be held to evaluate progress made on this recommendation and the formal meeting minutes will capture the evaluation.

OIG Audit Recommendation 2: *Enhance OCFI's strategic plan for implementing the FDIC's systemic resolution authorities by:*

- *Ensuring ongoing and planned projects and existing performance measures are integrated and linked to long-term goals and priorities, and*
- *Including aggressive, but achievable, milestones for measuring progress towards readiness and a mature OCFI organization.*

FDIC Response: The FDIC concurs with the recommendation. In conjunction with the FDIC's annual planning and budget process, the Office of Complex Financial Institutions (OCFI) will revise its current strategic plan around key business functions and priorities to ensure that ongoing and planned systemic resolution-related projects and performance measures are aligned to longer-term goals.

As part of this process, OCFI, the Division of Risk Monitoring and Supervision - Complex Financial Institutions (RMS-CFI) and the Division of Resolution and Receivership - Complex Financial Institutions (DRR-CFI) will each establish annual plans that will also include longer-term (2-3 year) strategic goals to address priorities that extend beyond the one-year Corporate planning horizon. The plans will reflect priorities established by the CCG. Progress will be reported by Memorandum to senior Division and Office management on a quarterly basis beginning March 31, 2014.

OIG Audit Recommendation 3: *Continue to build out and formalize coordination between OCFI and RMS regarding the Monitoring function.*

FDIC Response: The FDIC concurs with the recommendation and will take the following actions to continue to build out and formalize coordination between OCFI and RMS regarding

Appendix 5: Corporation Comments

the Monitoring function. Key aspects of OCFI and RMS-CFI coordination include the following:

- Strategic Planning: As noted in the planned activities to address the report's second recommendation, OCFI and RMS-CFI will coordinate and align strategic goals and priorities through the strategic planning process.
- Supervisory Risk and Resolution Activities Plans (SRRAPs): SRRAPs are jointly prepared planning documents to address supervisory and risk monitoring, as well as resolution planning efforts, for FDIC activities at each SIFI.
- SIFI Cross-Discipline Information Exchange (SCDIE): SCDIE are on-going, regular joint meetings with RMS and OCFI staff assigned to individual SIFIs to discuss issues and plan/coordinate FDIC activities.

Ongoing coordination efforts include:

- RMS-CFI on-site team are participating in Title I and IDI plan reviews led by OCFI (DRR-CFI staff will also participate);
- RMS-CFI onsite teams are participating in ongoing Title II strategy updates (DRR-CFI staff will also participate);
- RMS-CFI staff are participating in OCFI-led training; OCFI staff are also participating in RMS-CFI-led training;

OCFI and RMS-CFI are establishing written protocols regarding collaboration on information requests and other interaction with supervisory staff from other agencies and SIFIs to ensure protocols have been fully communicated to all parties. These written protocols will be finalized by February 28, 2014.

OIG Audit Recommendation 4: *Evaluate the sufficiency of staffing levels and skill sets for OCFI and other FDIC divisions and offices with resolution responsibilities—taking into consideration prior staff turnover—and determine a course of action for addressing identified gaps.*

FDIC Response: The FDIC concurs with the recommendation. As noted in the response to recommendation 3 above, RMS-CFI on-site teams and DRR-CFI staff will participate in Title I and IDI plan reviews, as well as the ongoing review of Title II strategies for specific institutions. These expanded, interdivisional interdisciplinary teams will greatly expand the resources and skill set mix available for resolution plan review activities. A resolution plan review cycle using these expanded teams will be helpful in assessing the skill set mix and staffing levels that may be needed going forward. Any request for additional staffing will be presented and justified as part of the FDIC Corporate mid-year budget adjustment process; this will serve as the assessment of staffing requirements and this assessment will take place in July 2014.

Appendix 5: Corporation Comments

OIG Audit Recommendation 5: *Strengthen and formalize protocols to ensure OCFI staff can efficiently discover, obtain, and share internal and external information.*

FDIC Response: The FDIC concurs with the recommendation. As noted in the response to recommendation 3, OCFI and RMS-CFI are establishing written protocols regarding collaboration on information requests and other interaction with supervisory staff from other agencies and with SIFIs. These written protocols will be presented to senior OCFI and RMS management by February 28, 2014. Once finalized, these protocols will be communicated to affected staff in OCFI and RMS-CFI no later than May 30, 2014.

OIG Audit Recommendation 6: *Establish timeframes and assign necessary resources for developing policies and procedures as soon as practical for key processes associated with the implementation of systemic resolution authorities.*

FDIC Response: The FDIC concurs with the recommendation. OCFI and other divisions and offices involved in implementation of systemic resolution authorities will update their policies and procedures manuals on at least an annual basis and more frequently should circumstances warrant. A plan for this review will be established no later than February 28, 2014. In addition, progress on this plan will be discussed at the quarterly meeting of the CCG when progress on achieving greater communication and communication on the wide range of matters involving complex financial institutions is evaluated by the CCG beginning no later than March 31, 2014.

Appendix 6: Summary of the Corporation's Corrective Actions

This table presents corrective actions taken or planned by the Corporation in response to the recommendations in the report and the status of the recommendations as of the date of report issuance.

Rec. No.	Corrective Action: Taken or Planned	Expected Completion Date	Monetary Benefits	Resolved:[a] Yes or No	Open or Closed[b]
1	The FDIC created the EMC-CFI to facilitate communication, coordination, consistency, and agreement throughout the FDIC regarding activities related to complex financial institutions. The EMC-CFI will meet quarterly to evaluate progress in defining and building consensus among corporate stakeholders regarding the activities for executing resolution strategies and the results will be recorded in the EMC-CFI's meeting minutes.	March 31, 2014	N/A	Yes	Open
2	OCFI will revise its current strategic plan around key business functions and priorities to ensure that ongoing and planned systemic resolution-related projects and performance measures are aligned to longer-term goals. As part of this effort, OCFI, RMS, and DRR will each establish annual plans that include long term strategic goals related to systemic resolution planning that reflect priorities established by the EMC-CFI.	March 31, 2014	N/A	Yes	Open

Appendix 6: Summary of the Corporation's Corrective Actions

Rec. No.	Corrective Action: Taken or Planned	Expected Completion Date	Monetary Benefits	Resolved:[a] Yes or No	Open or Closed[b]
3	OCFI and RMS will formalize collaboration regarding the Monitoring function through the strategic planning activities described under Recommendation 2. Additionally, OCFI and RMS will prepare supervisory and resolution activity plans and meet regularly to discuss and coordinate SIFI related activities.	March 31, 2014	N/A	Yes	Open
4	RMS and DRR will participate in reviews of resolution plans and Title II strategies for specific institutions. The use of these expanded interdivisional teams will help assess skill set and staffing needs and any needed adjustments will be addressed as part of the FDIC's mid-year budget review process.	July 2014	N/A	Yes	Open
5	OCFI and RMS will establish written protocols regarding information requests and interactions with supervisory staff from other agencies and SIFIs.	May 30, 2014	N/A	Yes	Open

Appendix 6: Summary of the Corporation's Corrective Actions

Rec. No.	Corrective Action: Taken or Planned	Expected Completion Date	Monetary Benefits	Resolved:[a] Yes or No	Open or Closed[b]
6	OCFI, in coordination with other FDIC divisions and offices, will develop a plan for ensuring that policies and procedures for key processes associated with the implementation of systemic resolution authorities are developed and updated.	February 28, 2014	N/A	Yes	Open

[a] Resolved – (1) Management concurs with the recommendation, and the planned, ongoing, and completed corrective action is consistent with the recommendation.
(2) Management does not concur with the recommendation, but alternative action meets the intent of the recommendation.
(3) Management agrees to the OIG monetary benefits, or a different amount, or no ($0) amount. Monetary benefits are considered resolved as long as management provides an amount.

[b] Recommendations will be closed when (a) Corporate Management Control notifies the OIG that corrective actions are complete or (b) in the case of recommendations that the OIG determines to be particularly significant, when the OIG confirms that corrective actions have been completed and are responsive.