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**Submitted via Internet:** executivecompensationcomments@do.treas.gov

November 19, 2008

Executive Compensation Comments  
Office of Financial Institutions Policy  
Room 1418  
Department of the Treasury  
1500 Pennsylvania Avenue, NW  
Washington, DC 20220

Dear Ladies and Gentlemen:

The American Bankers Association appreciates the opportunity to offer these comments on the executive compensation interim final rule applicable to participants in the Troubled Assets Relief Program (TARP) Capital Purchase Program (CPP). The ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members—the majority of which are banks with less than \$125 million in assets—represent over 95 percent of the industry's \$13.3 trillion in assets and employ over 2.2 million men and women.

The interim final rule is drawn from the executive compensation provisions of the Emergency Economic Stabilization Act of 2008 (EESA). Specifically, these provisions require that during the period the Department of the Treasury holds any equity or debt securities in a financial institution, that institution must:

- Certify that the contracts of the top five senior executives (SEO) do not encourage or reward unnecessary and excessive risk taking that threatens the value of the financial institution;
- Recover or “clawback” any bonus or incentive compensation paid to the top five senior executives based on statements of earnings, gains or other criteria that are later proven to be materially inaccurate;
- Not make any golden parachute payment to the SEOs; and
- Agree not to deduct for tax purposes executive compensation in excess of \$500,000 for each of the top five senior executives.

## DISCUSSION

### Compensation Committee Responsibilities

The interim final rule places significant corporate governance responsibilities on Board of Directors' compensation committees. Specifically, the interim final rule requires compensation committees to:

- Identify the features in the financial institution's SEO incentive compensation arrangements that could lead SEOs to take unnecessary and excessive risks that could threaten the value of the financial institution;
- Review, within 90 days after the purchase under the CPP, the SEO incentive compensation arrangements with the financial institution's senior risk officers or other personnel acting in a similar capacity, to ensure that SEOs are not encouraged to take such risks;
- Meet annually with the financial institution's senior risk offices to discuss and review the relationship between the financial institution's risk management policies and practices and the SEO incentive compensation arrangements; and
- Certify, in either the Compensation Discussion and Analysis (CDA) required under the federal securities laws for public companies or to the financial institutions' primary regulatory agency, that it has completed the required reviews of SEO incentive compensation.

Bank compensation committee members, like most bank boards of directors, are acutely aware of their fiduciary responsibilities to the corporation and its shareholders. High attendance rates and in-depth preparedness for compensation committee meetings, as well as the resolve of the committees to ask difficult questions regarding company compensation and bonus practices and to consult with expert third parties when necessary, are quite common in today's bank board rooms. And, most assuredly, compensation committees will tackle their new responsibilities under the TARP CPP program with the same degree of thoroughness and professionalism.

The requirement under EESA to root out "unnecessary and excessive risks that threaten the value of the financial institution" in incentive compensation plans, on its face, is too amorphous. While we continue to digest last week's Interagency Guidance on Meeting the Needs of Creditworthy Borrowers<sup>1</sup>, we do believe that some of that guidance may prove helpful to bank compensation committee members in reviewing their responsibilities under the CPP program. We particularly like the fact that the agencies have recognized the appropriateness of providing proper incentives to retain strong management.

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<sup>1</sup> Interagency Guidance on Meeting the Needs of Creditworthy Borrowers, November 12, 2008, available at: <http://www.fdic.gov/news/news/press/2008/pr08116.html>; We also note that excessive compensation is already prohibited as an unsafe and unsound banking practice. See Interagency Guidelines Establishing Standards for Safety and Soundness, Appendix A to Part 30, 12 CFR 30.

## Incentive Compensation

First, it is important to note that the “clawback” provision provided under the CPP is more expansive than that required under Section 304 of Sarbanes-Oxley Act. That provision requires the forfeiture by a public company’s chief executive officer (CEO) and chief financial officer (CFO) of any bonus and other similar remuneration during the twelve month period following a materially non-compliant financial report. The CPP clawback provision applies to all five SEOs, including the CEO and CFO for all participating companies, not just public companies; is not time bound (except to the extent Treasury holds a position in the financial institution); is not exclusively triggered by accounting restatements; and covers not only material inaccuracies relating to financial reporting but also material inaccuracies relating to other performance metrics used to award bonuses and incentive compensation.

The CPP clawback provision raises a number of questions regarding events that are beyond the control of the affected SEOs and management. For example, any new accounting guidance issued or revised after a participating financial institution has provided financial reports to the market and to appropriate regulatory authorities that later causes these reports to become materially inaccurate should not, in itself, require a company to recover incentive compensation previously paid to the covered SEO.

Second, under the Internal Revenue Code, certain incentive bonuses are generally deductible under Section 162(m)(4)(C) of the Code if the bonuses have been approved by shareholders and meet certain other requirements. Paragraph (5)(E), added under EESA to Section 162(m), does not exempt performance based compensation from the definition of “remuneration” and, thus, for those banks participating in the CPP, SEO incentive bonuses are not deductible to the extent that, together with the executive’s annual salary, the bonus exceeds \$500,000. We think this is unfortunate as SEOs should be appropriately incentivized, especially when those incentive plans have been approved by the shareholders.

We do not believe, however, that the term “remuneration” (and thus subject to the \$500,000 deductibility limits) includes stock bonus, profit sharing, and pension plans that are qualified under Section 401(a) of the Internal Revenue Code (IRC). We strongly believe that payments made under these plans should be deductible, but request clarification of this point.

## Golden Parachute Payments

The CPP expands the definition of “excess parachute payments” from change in ownership or control to include any payment to or for the benefit of the SEO made on account of severance from employment to the extent the aggregate present value of such payments equals or exceeds an amount equal to three times the SEO’s base amount. Severance includes involuntary termination or termination in connection with any bankruptcy filing. Thus, institutions participating in the CPP have additional limits on tax deductibility for any excess parachute payments. In addition, recipients of these payments are subject to a 20 percent excise tax on the amount received.

We do not believe that the definition of “excess parachute payment” includes monies contributed to plans qualified under IRC Section 401(a), as well as annuity plans, simplified employee pension plans and simple retirement accounts described in IRC Sections 403(a), 408(k) and 408(p), respectively, but request clarification of our understanding.

Sincerely yours,

A handwritten signature in cursive script that reads "Sarah A. Miller". The signature is written in black ink and is positioned below the "Sincerely yours," text.

Sarah A. Miller