CENTER FOR CAPITAL MARKETS COMPETITIVENESS

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November 25, 2009

Ms. Jennifer J. Johnson
Secretary,
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Proposed Guidance on Sound Incentive Compensation Policies
Docket No. OP-1374

Dear Ms. Johnson:

The U.S. Chamber of Commerce is the world's largest business federation, representing more than three million businesses and organizations of every size, sector, and region. The Chamber created the Center for Capital Markets Competitiveness ("CMCC") to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy. To achieve this objective, it is an important priority of the CMCC to advance an effective and transparent corporate governance structure. The CCMC welcomes this opportunity to comment on the Guidance on Sound Incentive Compensation Policies ("proposed guidance") proposed by the Board of Governors of the Federal Reserve System ("Federal Reserve").

Strong corporate governance is a cornerstone of fundamental business practices. Effective relationships and dialogue between shareholders and directors is needed for the long-term viability and profitability of a company or financial institution. The setting of policies to determine compensation is an important part of that governance process.

Earlier this year, the Chamber wrote to Treasury Secretary Timothy Geithner with a set of principles on corporate governance and compensation. Those principles are:

- Corporate governance policies must promote long-term shareholder value and profitability but should not constrain reasonable risk-taking and innovation.

- Long-term strategic planning should be the foundation of managerial decision-making.

- Corporate executives' compensation should be premised on a balance of individual accomplishment, corporate performance, adherence to risk management, and compliance with laws and regulations, with a focus on shareholder value.

- Management needs to be robust and transparent in communicating with shareholders.

In presenting these principles, the Chamber also stated: "[t]hese principles provide a template for policies that would allow for reasonable risk taking, continued innovation, the ability to acquire and retain talent and protect investor rights".

The safety and soundness of our financial institutions are of fundamental importance to our economy. Capital formation is a key factor in job creation and a failure to have functioning and efficient markets will adversely impact long-term economic growth.

However, the potential unintended consequences that could flow from the proposed guidance also need to be weighed. Potential adverse impacts upon financial institutions need to be addressed so that harmful broad macro-economic consequences can be avoided.

Retention and Acquisition of Talent

Human capital is the operating infrastructure of a financial institution. The quality of the workforce and ability to attract talent are long-term indicators of the financial institutions ability to be successful and secure profitability. Appropriate compensation practices that allow employees to engage in reasonable risk taking and long-term decision making are of great importance. Narrow compensation policies and practices will drive away talent, degrade the foundation and long-term viability of a firm. The Treasury Department's administration of Troubled Asset Relief Program ("TARP") compensation policies may provide such an example.

In submitting a comment letter on the Treasury Department's Standards for Compensation and Corporate governance the Chamber stated:

> **The evaluation of compensation and governance policies for TARP companies should be done with an eye to providing those companies with the tools and talent needed to be successful over the long-term. TARP recipients must be able to compete in the marketplace. To do so, they must be able to attract and retain needed talent. If their compensation programs are not competitive, their ability to leave TARP will be impaired. The unfortunate reality is that TARP companies are already at a disadvantage. There have been press reports throughout the year have indicated that foreign firms such as Deutsche Bank, UBS and others have been drawing talented individuals away from TARP firms....Therefore, the principles should be amended to contain a principle on the competitiveness of TARP companies.**

Recent press reports (see attachments) have recorded the flight of talent that has occurred before and since the Treasury Department's Special Master Kenneth Feinberg started to issue his compensation decisions for TARP firms. The *Washington Post* has reported that in two firms, close to a majority of the top 25 most highly paid executives left before the Special Master ruling was even announced. Several days ago, it was reported in *Bloomberg News* that Special Master Feinberg stated that he is "very concerned" that his rulings will drive talent away from companies.

Actions have consequences and the competition for talent is fierce. Employees can be lured away by direct competitors, global firms, or different industries. Accordingly, a flight of talent from banks to private equity firms, mutual funds, hedge funds or global firms may create a brain drain that can be destructive to the banks in which compensation will be regulated through the proposed guidance. Such an exodus of skill, intelligence and experience can quickly denude a financial institution of its talent base and impact its survivability.

Accordingly, while the proposed guidance discusses an appropriate balance between risk taking and compensation, there has not been enough of a discussion or development of guidance to address the competition of talent or the impacts of a brain drain from a financial institution. An exit of talent can be as devastating as excessive risk, yet the proposed guidance remains silent on the issue. Accordingly, the proposed guidance should be updated to include principles on talent acquisition and retention.

The Role of the Director and Shareholder

It goes without saying that the Federal Reserve's supervisory role in the safety and soundness of covered financial institutions is paramount. However, it must not be forgotten that directors and shareholders share a unique and vital responsibility in the management of a financial institution.

A one size fits all approach, besides destroying the human capital of a firm as discussed above, would emasculate the ability of directors and shareholders to perform their legally obligated management duties. This is clearly the case if a formulistic approach where ever to be used. However, a heavy handed use of the proposed guidance could have the same effect.

Shareholders and directors can, within the regulatory framework choose the governance and compensation structures that work best for that financial institution. This will lead to a diversity of structures and practices that can best suit the financial institution. While this may provide firms with a competitive edge, it also creates a dynamic capital markets system. A one size fits all approach will destroy that diversity and inhibit the efficiency of our capital markets adversely impacting the economy overall. Accordingly, in its reviews, the Federal Reserve should work closely with directors and shareholders to evaluate and strengthen the managerial aspects of that relationship. The Federal Reserve should be sensitive not to undercut the director shareholder dialogue and tailor the proposed guidance and its implementation to reinforce it.

Small and Regional Banks

The proposed guidance states that the Federal Reserve will conduct a special horizontal review of incentive compensation practices for large complex banking organizations and a review of incentive compensation at other banking organizations.

The CCMC believes that a special study should concentrate on small and regional banks. The requirements to comply with the proposed guidance would appear to be more burdensome for smaller and regional banks. These banks also face different problems and issues than other institutions and it would be prudent to concentrate a special focus on their needs. The purpose of the outcome should be to adapt the proposed guidance that can work for smaller and regional banks and effectuate the goals of the Federal Reserve.

Conclusion

The CCMC once again would like to thank the Federal Reserve for the opportunity to comment on the proposed guidance. The CCMC believes that the proposed guidance should be amended to include principles on competition and the ability of banks to attract and retain talent. Additionally, the role of directors and shareholders should be preserved and strengthened, while the needs of small and regional banks should be understood and addressed. Without question, financial institutions should avoid excesses that imperil the long-term viability of the firm. However, the Federal Reserve's policies must be crafted to allow financial institutions to flourish. Profitable stable financial institutions will insure vibrant capital markets which are the engines and providers of long-term job growth. Appropriate guidance can assist in the efficient operation of capital markets, while improper rules or enforcement can create underperformance values that will harm economic growth.

Sincerely,

Thomas Quaadman
Executive Director for Financial Reporting
and Investor Opportunity
Center for Capital Markets Competitiveness
U.S. Chamber of Commerce

Bloomberg.com

Feinberg 'Concerned' Pay Cuts Could Drive Out Talent (Update3)

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By Ian Katz

Nov. 12 (Bloomberg) -- **Kenneth Feinberg**, the Obama administration's special master for executive compensation, said he is "very concerned" about the possibility his pay cuts may drive talent away from companies bailed out by U.S. taxpayers.

"I'm very cognizant of the concerns expressed by these companies," Feinberg said today in Washington at an event held by Bloomberg Ventures, a unit of Bloomberg LP, parent of Bloomberg News. "The law makes it clear that the determinations I render are designed, first and foremost, to make sure those companies thrive and that the taxpayers get their money back."

Feinberg has ordered pay cuts averaging 50 percent for the top 25 executives at **Citigroup Inc.**, Bank of **America Corp.**, American International Group Inc. and four other companies that took U.S. bailout money. He will rule on pay structures covering the next 75 highest-paid employees at those firms by year-end.

"Maybe I've struck the right balance," Feinberg said, referring to criticism that he has been too harsh and too easy on executives. "Hopefully some of this will percolate into the private sector, we'll have to see."

The U.S. will track possible executive defections by seeking from the seven companies data on comparative pay, by obtaining independent information and requesting "anecdotal evidence of vacancies and concerns about losing people," he said.

"You cannot help but be sensitive to the political realities," Feinberg said. "You can't have blinders on." He added that there was "no vindictiveness in my decisions. There's no revenge."

AIG'S Benmosche

Feinberg said AIG Chief Executive Officer **Robert Benmosche**, who took over the insurer in August, had "expressed his concern that compensation keep his people on board and that the company thrive." Feinberg told reporters he has met with the chief executive "one or two times over the last few months."

Benmosche yesterday wrote to AIG employees, saying he remains "totally committed" to leading the insurer after media reports suggested he told the board he may step down because U.S. pay caps hurt his ability to retain staff.

Benmosche released the letter after the Wall Street Journal said Nov. 10 that he told directors last week he might resign because of U.S. limits on employee compensation. Benmosche, who came out of retirement to lead New York-based AIG, said he is "frustrated" with limits on what the company can pay its top 100 executives.

Phibro Sale

Citigroup last month agreed to sell its Phibro LLC energy- trading unit to Occidental Petroleum Corp. to avoid a showdown with Feinberg over a proposed $100 million pay package for **Andrew Hall**, Phibro's chief executive officer.

"It was Citigroup that made the determination that it did not want Phibro and its traders to be subject to my jurisdiction," Feinberg said. "They made the voluntary decision to spin that unit off." Feinberg noted that he had "expressed reservations" that Hall's pay might constitute "excessive risk."

Phibro, based in Westport, Connecticut, made money in each fiscal year since 1997. New York-based Citigroup, which had a record $27.7 billion net loss last year, accepted a price of about $250 million, less than Phibro's average annual earnings.

Goldman Sachs Group Inc., Morgan Stanley and JPMorgan Chase & Co.'s investment bank, all exempt from Feinberg's oversight, will hand out a combined $29.7 billion in bonuses, according to analysts' estimates. That's up 60 percent from last year and more than the record $26.8 billion in 2007. The companies are the biggest banks to exit the Troubled Asset Relief Program.

To contact the reporter on this story: **Ian Katz** in Washington at **ikatz2@bloomberg.net**.

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The Washington Post

Top employees leave financial firms ahead of pay cuts

Grass is greener where bonuses are sky-high

By Tomoeh Murakami Tse and Brady Dennis
Washington Post Staff Writer
Friday, October 23, 2009

NEW YORK -- Even before the Obama administration formally tightened executive compensation at bailed-out companies, the prospect of pay cuts had led some top employees to depart.

The administration had tasked Kenneth Feinberg, the Treasury Department's special master on compensation, to evaluate the pay packages of 25 of the most highly compensated executives at each of seven firms receiving exceptionally large amounts of taxpayer assistance.

But Thursday, he ruled only on slightly more than three quarters of the pay packages that were to be under his purview. The balance reflected executives who have left since he began his work in June or will be gone by the end of the year.

Many executives were driven away by the uncertainty of working for companies closely overseen by Washington, opting instead for firms not under the microscope, including competitors that have already returned the bailout funds to the government, according to executives and supervisors at the companies.

"There's no question people have left because of uncertainty of our ability to pay," said an executive at one of the affected firms. "It's a highly competitive market out there."

At Bank of America, for instance, only 14 of the 25 highly paid executives remained by the time Feinberg announced his decision. Under his plan, compensation for the most highly paid employees at the bank would be a maximum of $9.9 million. The bank had sought permission to pay as much as $21 million, according to Treasury Department documents.

At American International Group, only 13 people of the top 25 were still on hand for Feinberg's decision.

Feinberg did not detail how he plans to tackle the politically sensitive issue of nearly $200 million in bonuses due in March to employees at AIG Financial Products, the unit whose complex derivatives contracts led to the collapse of AIG last fall. Feinberg has urged the company to find a way to scale back the bonuses in hopes of preventing another round of public outrage.

In his written ruling Thursday, Feinberg noted that the firm had played a role "in the events necessitating taxpayer intervention," and concluded that AIG Financial Products employees should be paid only what their base salaries were on Dec. 31, 2008. In addition, he said that he continues to urge company officials to recoup the bonus payments that some Financial Products employees pledged to repay earlier this spring but did not. Until that issue is resolved, he wrote, employees should receive no pay in addition to their base salaries.

That news drew scorn Thursday from employees at AIG Financial Products who said they had repeatedly offered to rework their pay arrangements but that Feinberg was unwilling to work with them.

"He has zero credibility with FP employees at this point," said one employee, who was not authorized to speak on the record. "It's a very demoralized workforce."

Several of the companies said they had already been making changes in their compensation plans to better link executive pay to performance and that their compensation committees had worked closely with Feinberg's team to come up with a final plan reflecting that principle.

"We've been going down that road," said Bob Stickler, a Bank of America spokesman. "This is really more of the same." But he also said that the ruling "does go pretty far and there are competitive issues we're worried about."

On Wall Street, reaction to Feinberg's ruling was swift, with some executives arguing that it will further handicap the most troubled firms by driving away top employees while making companies unwilling to promote rising stars for fear of bringing them to Feinberg's attention.

But Nomi Prins, a former Goldman Sachs employee, said Feinberg's rulings are unlikely to change the culture of bonuses on Wall Street.

"I don't think Wall Street is afraid of this at all," said Prins, author of "It Takes a Pillage: Behind the Bailouts, Bonuses, and Backroom Deals from Washington to Wall Street."

"It's going to affect a small portion of a small portion of the industry. It won't have a lasting impact."