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November 26, 2009

Via Electronic Mail

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

Re: Docket No. OP-1374

Dear Ladies and Gentlemen:

Amalfi Consulting appreciates the opportunity to comment on the Board's Proposed Guidance on Sound Incentive Compensation Policies published in the Federal Register on October 27, 2009. Amalfi Consulting is a national, independent firm providing compensation consulting services exclusively to banking organizations.

Competitive Considerations
A common theme we are hearing from our clients about the Board's proposed guidance is that it creates competitive disadvantages to covered institutions relative to banking organizations that are not subject to Federal Reserve regulation and other types of unregulated organizations, such as mortgage brokers. The Board notes that supervisory action can play a critical role in addressing the "first mover" problem by reducing an organization's concerns that modifications to incentive compensation arrangements might have adverse competitive consequences. While the Board's proposal covers a significant number of institutions, it still leaves out those competing entities that are either banks not regulated by the Federal Reserve or are not banking organizations. Thus the proposed guidance imposed on covered institutions results in competitive disadvantages underlying the first mover syndrome. For example, a bank with a significant mortgage operation would be at a competitive disadvantage under the proposed guidance as the resulting incentive compensation would work to motivate employees to terminate their employment and go to work for a non-regulated mortgage company.

There are no easy answers to creating a level playing field in all areas where banking institutions compete with non-banks and one another for personnel talent. A joint guidance by all Federal bank regulatory agencies would be an effective first step in balancing competition within the banking industry but would not address competition from outside the industry. It may be worthy of legislative initiative to bring such common activities under a common regulatory purview. At present, the operation of the proposed guidance could potentially act to further weaken banking organizations through the potential dislocation of talent from one banking organization to another institution as a result of inconsistent application.

Clarification of Scope
Another common theme we are hearing is uncertainty as to which individual banks are considered "supervised by the Federal Reserve". For instance, are compensation policies for employees of a state-chartered, non-member bank owned by a one-bank holding company subject to the proposed

3600 American Boulevard West * Suite 110 * Minneapolis, MN 55431
Phone 952-893-6732 * Toll Free 866-280-3720 * Fax 952-893-6770 * www.amalficonsulting.com

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guidance? The Board could alleviate confusion within the industry by adding specific examples of the scope of the guidance as it applies to the myriad organizational structures within the banking industry.

Subjectivity of Application

The proposed guidance recognizes the vast differences in risk profiles, activities and compensation practices across the banking spectrum and offers that compliance with the broad principles in the guidance will be assessed on a case by case basis during the regular examination process. Supervisory findings will be included in the relevant report of examination or inspection and will be incorporated into an organization's supervisory rating. Enforcement action is possible where supervisors determine that incentive compensation arrangements, risk management or governance processes pose a risk to the safety and soundness of an organization.

Since the guidance is not adopted as a rule and is quite broad and principles-based, it appears that the measure of an individual institution's compliance will therefore be subjective, based on a determination by different supervisory staff from institution to institution. We believe the Board should give additional attention to description of compliant action on the part of covered organizations.

In other words, one institution's view of risk will often be different than another institution's view of risk. As such, their relative compliance with the proposed guidance will potentially be significantly different. Why is this important? The resulting incentive compensation plan designs of each organization will, based on their own assessment of risk, be quite different. This can potentially act to undermine consistency in principled application of the proposal. As a result, the "compliant incentive plans" from one institution to another could very dramatically and result in a dislocation of employees from one organization to another.

We suggest that if the Board has in mind minimum levels of changes in incentive compensation plan design, it could help institutions address what they must do to be in compliance. Are there any tenants of incentive plan design that the Board considers as minimally acceptable? If so, examples of this could be extremely helpful and beneficial to the banking community.

What we can tell you is that in working with our banking clients, in complete opposition to the "first mover" behavior that the Board desired to address, many community banks are taking a cautious view of this proposed guidance. Many organizations are waiting to see what the Board releases after the comment period or after seeing what is publicly disclosed after the large complex banking organizations submit their plans to the Board on February 1, 2010.

Application of IRC Section 409A

One of the four methods for attaining balance between compensation and risk prescribed by the Board is "Deferral of Payment". As the name suggests, this method involves the deferral of incentive compensation payments over a period of time. IRC Section 409A includes many complex provisions relative to deferred compensation from a taxation standpoint, including onerous financial consequences for non-compliance. As a practical matter, we suggest that the Board describe how the compensation deferral suggested in the proposed guidance will interact with Section 409A. It would also be instructive to know whether the Board has consulted with Treasury on whether deferrals resulting from the Board's proposed guidance must to be fully compliant with Section 409A or whether exceptions may become available by regulation as were provided under the Treasury's June 15, 2009 Interim Final Rule for TARP institutions.

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Potential Conflict of Guidance with Contract Law
Under Principal #1, Balanced Risk-Taking Incentives, the Board suggests, "*Banking organizations should carefully consider the potential for "golden parachutes" and the vesting arrangements for deferred compensation to affect the risk-taking behavior of employees while at the organizations.*" We question how this guidance may interact with contract law. In particular, where an existing deferred compensation arrangement provides for accelerated vesting upon a termination event (e.g., a change-in-control), unilateral amendment by the employer may not be practicable. Employment arrangements and deferred compensation arrangements are most often modified only by mutual agreement of the contracting parties. As such, if the executive does not agree to amend an existing employment or deferred compensation arrangement, the Board's suggested approach is problematic, at best.

Strong Corporate Governance – Senior Executive Clarification
As it relates to corporate governance, the proposed guidance suggests that the board of directors, or the compensation committee of the board, approve the incentive compensation arrangements of senior executive officers. We suggest that a clear definition of the term senior executive officer be provided in the final guidance. While the general notion is a common sense, principled based one, the definition of senior executive officer can be subjective and vary widely from institution to institution. The Board could adopt a definition similar to the *named executive officer*, or, *select executive officer* from the SEC and TARP definitions which generally includes up to five executives. Any clarification would be useful given that many compensation committees historically have been limited to evaluating only the CEO and/or the CEO and EVP-level positions.

Thank you for affording us the opportunity to comment.

Sincerely,

Todd A. Leone
President and Founder
Amalfi Consulting, LLC
Direct: 952.893.6711
Email: todd.leone@amalficonsulting.com