

# THE FINANCIAL SERVICES ROUNDTABLE



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November 24, 2009

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: Proposed Guidance on Sound Incentive Compensation Policies**

Dear Ms. Johnson:

The Financial Services Roundtable<sup>1</sup> (Roundtable) appreciates this opportunity to comment on the Proposed Guidance on Sound Incentive Compensation Policies of October 22, 2009 (Guidance). We support the Guidance's principles-based approach and applaud the Federal Reserve Board's (Board) decision not to issue blanket requirements or prohibitions. However, we have identified several areas of concern, as described below.

### **One Size Does Not Fit All**

The Roundtable supports the Guidance's principles-based approach. Financial services is a diverse, complex industry in which one size almost never fits all. As such, the Board chose to enumerate three key principles. The Roundtable supports this approach because it allows each institution to tailor their internal policies and procedures to adhere to these principles. Given the breadth and complexity of the industry, we urge that this latitude be as broad as prudently possible. Firms should have discretion to meet the core principles in the manner best calibrated to their particular shareholders and employees. This flexible approach will best promote safety and soundness both within individual institutions and across the broader market. Below, we identify several specific areas in which we believe the Board should provide broad discretion:

- **Incentive Compensation**: The Roundtable believes that firms must be able to design pointed compensation programs capable of attracting top talent. If application of the Guidance becomes overly rigid and firms are unable to implement competitive compensation arrangements, the best suited employees will migrate to less-regulated sectors. Accordingly, the Roundtable encourages the Board to allow firms significant

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<sup>1</sup> The Financial Services Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Roundtable member companies provide fuel for America's economic engine, accounting directly for \$84.7 trillion in managed assets, \$948 billion in revenue, and 2.3 million jobs.

discretion to design compensation programs that, while fulfilling the core principles, are geared towards their own specific recruitment and retention needs.

- Management's Discretion of Awards: Most incentive compensation plans permit broad discretion to management to approve specific awards based on individual, group and company performance. The Guidelines should not require documentation that undermines management's ability to make subjective decisions based on all factors considered relevant to an award. The guidelines should also reflect that although risk is a factor, management (with board oversight) must be able to make individual decisions based on the relevant market and geographical factors in order to attract and retain talented employees.
- Risk Management and Controls: Risk management requirements should be tailored to the situations of individual firms. Financial services institutions currently have risk management programs of varying scope and effectiveness. If heightened requirements are imposed on firms with already-effective risk management regimes, the result will likely be unnecessary bureaucracy and corporate waste. Heightened requirements would be more burdensome for responsible firms, creating new inefficiencies.

Moreover, some institutions are naturally exposed to relatively low levels of risk. It would be unwise to impose the same risk management requirements on low-risk firms as on their riskier competitors. We fear that this one-size-fits-all approach would result in high compliance costs and little benefit to low-risk firms or their customers. We therefore encourage you to adopt an approach to risk management that takes into account current risk management procedures at individual firms. Institutions should be encouraged to use existing risk and control assessments and mitigation factors as tools to review risks related to incentive comp and should not be required to develop new analysis. Many institutions have gone through this for Basel II, Sarbanes-Oxley and other purposes so banks should be given reasonably broad discretion to use existing analysis to test for risk related to incentive compensation. This approach would better suit both the industry and adhere to the principles of the Guidance.

- Board of Directors' Experience/Involvement: *[Note that "Board" is a defined term referring to the Federal Reserve.]* The extent to which the Board of Directors is involved in firms' risk management and compensation practices varies across the industry. The Roundtable is concerned that the Guidance will mandate high levels of intervention by each firm's Board of Directors in all situations. We believe that such a blanket imposition could undermine the Guidance's purposes in a number of ways. For instance, many firms have highly trained, experienced management personnel who are responsible for all risk management, capital and liquidity planning and incentive compensation related activities. The level of expertise and involvement of Directors should not be required to supplant that of management. The Board of Directors and its compensation committee have responsibility to exercise its business judgment in assessing the firm's compensation arrangements. To do so, they should have the capability to understand and assess the

information they receive and determine if they wish additional resources, whether from within the firm, externally or both, to assist them in the exercise of their responsibilities. We therefore encourage the Board to consider what level of involvement by a Board of Directors would best suit each individual firm.

Consistent with the above paragraphs, the Roundtable encourages the Board to provide its examiners with appropriate training and oversight in order to guard against overly-rigid or formulaic application of the Guidance. We further encourage the Board, in applying such guidance, to take into account that: 1) one size does not fit all, 2) formulaic requirements would be counterproductive, and 3) formal or informal industry-wide mandates regarding incentive compensation or specific results, programs or plans at individual institutions will not achieve the underlying goals associated with the principles. All reviews and examinations should reflect these principles.

### **Incentive Compensation Information Should Not Be Publicly Disclosed**

Disclosures on incentive compensation agreements are necessary for regulators to develop a clear image of practices on the micro and macro levels, which in turn is necessary to implement effective regulation. Public financial services firms vigorously compete for talent, both amongst themselves and with private companies. We strongly urge that the confidentiality of incentive compensation information disclosed to the regulators be consistent with existing disclosure regimes, like the SEC's executive compensation disclosure rules. To disclose firms' compensation arrangements of employees, other than those already required to be disclosed, would greatly impede their competitive positions—private firms would have full access to information regarding public firms' compensation structures with no reciprocal transparency requirement. Additionally, firms incur considerable expense to design attractive, risk-conscious incentive compensation arrangements.

### **Staff Should be Excludable From Coverage**

The current guidance applies to (1) senior executives, (2) individuals who expose the firm to material risk and (3) groups that also expose the firm to material risk. We are concerned that the Guidance can be interpreted to apply to certain staff, due to the nature of their positions. As such, the Roundtable recommends that the Board permit institutions to focus the risk assessment on persons reasonably determined by management (with broad oversight) to be in these three categories and not require detailed analysis and documentation for incentive compensation decisions for all employees. The guidelines should also recognize risk mitigation and controls in determining the number and groups of employees that are considered to be in these categories.

### **Federal Regulators Should Coordinate Effectively**

The Roundtable is concerned that its member institutions could be subject to incompatible or conflicting regulations from various regulators. While we are confident that the Board would

implement the Guidance in a consistent manner, we nonetheless appreciate that it can be difficult to comply with different sets of instructions emanating from different agencies. For example, the discussion in the guidance suggesting limitations or bans on the use of 'golden parachutes' and certain deferred compensation vesting arrangements is contrary to a principles-based approach. It is also contrary to comments made by other regulators about the need to provide for the forfeiture of deferred compensation. In short, the lack of consensus on this issue shows that, indeed, no one size fits all and that proscriptive rules may result in unintended consequences.

Additionally, the Securities and Exchange Commission (SEC) plans to address disclosure obligations and guidance on compensation. As public companies, our members will have to comply with the new SEC rule in its final form. As such, we recommend that the Board should also coordinate with the SEC to ensure that its guidance is in line with what the SEC will require of all public companies.

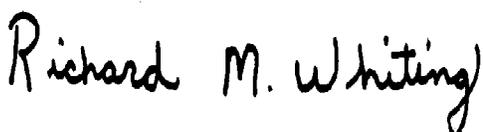
Accordingly, the Roundtable encourages the Board to include in the final Guidance a statement explaining how the Board will coordinate, collaborate, and harmonize with other regulators in application of the Guidance.

#### **Compliance and Risk Management Employees**

One issue that is not directly covered in the guidelines is the extent to which compliance and risk management employees should be under incentive compensation plans that are separate from business unit plans. Although incentive compensation decisions for compliance and risk employees should not incent them to compromise the company's risk and compliance standards to promote business unit profitability, management (particularly the senior risk/compliance officer) should have broad discretion to make awards to these employees based on overall performance. These awards should be within the same general incentive compensation plan and not within an individual incentive compensation plan.

Thank you again for the opportunity to share our views with you on this subject. If you have any questions, please feel free to contact me or Melissa Netram at 202-289-4322.

Sincerely,



Richard Whiting  
Executive Director and General Counsel