The Clearing House Association, L.L.C.

NPR on Incentive Compensation (Dodd-Frank Section 956) (Docket No. R-1410)

On September 14, 2015, Jeremy Newell, Angelena Bradfield and Paige Pidano from The Clearing House Association, L.L.C. (the "Clearinghouse"), Kieran Fallon from PNC Bank, Deanne Schubring from M&T Bank, and Marc Trevino and Josh Lerner from Sullivan & Cromwell met with Michael Solomon, Meg Donovan, and Teresa Scott from the Division of Banking Supervision and Regulation and Michael Waldron from the Legal Division concerning developments in incentive compensation practices since the financial crisis and the attendees' views on the interagency rulemaking or guidance required to be issued pursuant to section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

The attendees discussed conclusions they reached from an anonymous survey of 16 Clearinghouse members on incentive compensation issues. According to the attendees, the survey illustrates changes in incentive compensation practices for executives that have occurred since 2008. The results of the survey pointed to a number of conclusions: 1) there has been a move from annual to longer-term performance measures; 2) the use of leverage has decreased, 3) there has been increased attention on risk-adjusting incentive compensation through both ex ante and ex post measures, and increased involvement of the risk function in all aspects of incentive compensation; and 4) there has been an increase in the use of forfeiture/reduction/clawback of incentive compensation by institutions.

The attendees argued that the larger point these changes exemplify is that there has been rapid evolution of incentive compensation practices since 2008, some driven by institutions and some by regulators. There has not yet been an opportunity to observe the efficacy of the various aspects of this rapid evolution. The issuance of inflexible interagency rules on incentive compensation could act to "freeze" inappropriate requirements in place with potentially significant unintended consequences. This could impact the ability of financial services firms to attract and retain talent, since these firms already compete for talent against a wide variety of firms that would not be subject to these requirements, including technology companies. The attendees would prefer that any interagency rule or guidance retain flexibility for firms, such as through the use of principles rather than specific requirements.

The attendees also asked that the regulators be cognizant of not placing what should be management responsibilities with respect to incentive compensation onto boards of directors or board committees, whose role should properly be oversight of compensation at their firms. Other specific requirements that the attendees thought would be problematic included 1) a requirement to use performance bonds in incentive compensation; 2) "European-style" absolute limits on variable compensation as a percentage of base salary; 3) approaches to the "excessive compensation" concept that differ significantly from the existing interagency guidelines; and 4) extraordinarily long deferral of incentive compensation.