



**July 22, 2016**

*Via Electronic Mail*

Robert deV. Frierson  
Secretary  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> Street & Constitution Avenue, N.W.  
Washington, DC 20551  
Docket No. 1536  
RIN No. 7100 AE-50

Legislative and Regulatory Activities Division  
Office of the Comptroller of the Currency  
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Washington, DC 20219  
Docket ID OCC-2011-0001

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Executive Secretary  
Attention: Comments, Federal Deposit Insurance  
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Federal Deposit Insurance Corporation  
550 17<sup>th</sup> Street, N.W.  
Washington, DC 20429  
RIN 3064-AD86

Alfred M. Pollard  
General Counsel  
Attention: Comments/RIN 2590-AA42  
Federal Housing Finance Agency  
400 7<sup>th</sup> Street, S.W.  
Washington, DC 20219

Gerard S. Poliquin  
Secretary of the Board  
National Credit Union Association  
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Brent J. Fields  
Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, DC 20549

Re: Notice of Proposed Rulemaking on Incentive-Based Compensation Arrangements (Docket Nos. OCC-2011-0001, 1536, RIN No. 7100 AE-50, RIN 3064-AD86, RIN 2590-AA42) – Comment Letter on the Notice of Reproposed Rulemaking on Incentive-Based Compensation Arrangements

Ladies and Gentlemen:

We respectfully submit these comments on behalf of UBS Group AG ("UBS") in response to the request for comment on the repropose rules (the "Proposed Rulemaking") implementing the provisions of Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Section 956").<sup>1</sup> We appreciate the difficulty of the task facing the agencies in implementing Section 956 and we appreciate the great deal of effort that has gone into the Proposed Rulemaking.

Though we are participating in comment letters that will be submitted by the Institute of International Bankers (IIB), the Securities Industry and Financial Markets Association (SIFMA), and The Clearing House Association L.L.C. (TCH), we want to highlight an issue of particular importance to UBS and for which our perspective can be especially useful to the agencies.

The Proposed Rulemaking in Section 236.7(a)(4)(i) mandates for Level 1 and Level 2 covered institutions that the incentive-based compensation paid to senior executive officers and significant risk-takers

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<sup>1</sup> See Incentive-based Compensation Arrangements, as adopted by the Board of Governors of the Federal Reserve (<http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20160502a2.pdf>). For convenience, we cite only to the Federal Reserve release. Section citations herein are to that release.

include substantial portions of both deferred cash and equity-like instruments. In this respect, the Proposed Rulemaking in Section 236.2(p) defines "equity-like instrument" as: (1) equity in the covered institution or any affiliate of the covered institution; or (2) a form of compensation (i) payable at least in part based on the price of the shares or other equity instruments of the covered institution or of any affiliate of the covered institution, or (ii) that requires, or may require, settlement in the shares of the covered institution or any affiliate of the covered institution. The Proposed Rulemaking does not define "deferred cash," and even though the Proposed Rulemaking indicates that deferred cash can be structured to share many attributes of a debt instrument, there is no indication that deferred cash can be settled other than in cash.

UBS is subject to strict home country rules and regulations governing incentive compensation. In Switzerland, the Financial Market Supervisory Authority (FINMA) is heavily involved in regulating compensation arrangements of banking entity employees. In this respect, on January 1, 2010, a FINMA-issued circular setting forth ten minimum standards for remuneration schemes of financial institutions came into effect.<sup>2</sup> In many respects the goals of the FINMA regulations are aligned with the Proposed Rulemaking and the FINMA standards recognize the importance of compensation schemes in the support of the long-term success and stability of the company while also considering the influence on capital, liquidity and risk to ensure appropriate risk taking.

In compliance with FINMA's standards on remuneration schemes, a substantial portion of the incentive-based compensation paid to UBS's employees whose total compensation exceeds CHF/USD 300,000 (which includes UBS's senior executive officers and key risk takers) is subject to mandatory deferral mechanisms including the UBS Equity Ownership Plan (the "EOP") and the UBS Deferred Contingent Capital Plan (the "DCCP").<sup>3</sup>

- Under the EOP, awards are granted in the form of notional shares which are based on the value of UBS shares. As outlined in Section 956, these awards create alignment with our shareholders.
- EOP awards granted to Asset Management employees are granted in cash settled notional funds. The notional funds support the alignment of portfolio managers and other Asset Management employees with the investors in our funds.<sup>4</sup> We note that these notional funds are not based on the price of shares or other equity instruments of UBS and they are not settled in UBS shares.
- Under DCCP, employees are awarded notional additional tier 1 (AT1) instruments, which can be settled in the form of a cash payment or a perpetual marketable AT1 instrument at the discretion of UBS. Awards granted under the DCCP forfeit if our phase-in Basel III common equity tier 1 capital ratio falls below 10% for Group Executive Board members and 7% for all other employees. In addition, awards are also forfeited if a viability event occurs, that is, if FINMA provides written notice to UBS that DCCP awards must be written down to prevent an insolvency, bankruptcy or failure of UBS or if UBS receives extraordinary support from the public sector that FINMA determines and confirms in writing is necessary to prevent such an event.

Our EOP and DCCP plans are fundamental in creating alignment with our equity and debt investors (and our fund investors in the case of Asset Management employees) and in supporting long-term sustainable results that effectively balance risk and reward. These plans have been in place for

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<sup>2</sup> FINMA Circular 2010/1, Remuneration Schemes, Minimum standards for remuneration schemes of financial institutions.

<sup>3</sup> We believe that the UBS plans currently impose the longest average deferral duration in the industry. Even though our comment letter focuses on the form of deferral requirements, we ask the agencies to consider allowing an offset of such longer vesting periods against the proposed 7-year clawback requirement.

<sup>4</sup> This compensation structure is consistent with the *Guidelines on Sound Remuneration Policies Under the UCITS Directive and AIFM* issued by the European Securities and Markets Authority (dated March 31, 2016).



numerous years and have been implemented in coordination with FINMA. While we appreciate that regulation of compensation arrangements is important, we believe that mandatory requirements as to the form of deferral are unnecessary and overly prescriptive, and can lead to unnecessary and unintended results.

In particular, the Proposed Rulemaking requirements suggest that the EOP awards granted to our Asset Management employees would not constitute "equity-like instruments" as the value of the awards or the payment thereof is not linked to the price of UBS stock, a result that would place the continued use of these notional fund grants that are aligned with our fund investors in jeopardy. Further, and even more concerning, our DCCP plan awards, which are fundamentally marketable subordinated debt instruments in the additional tier 1 category, do not seem to be envisioned by the Proposed Rulemaking as they may be settled in a marketable debt instrument rather than in cash.<sup>5</sup>

Such outcomes should not be the intent of the agencies and we respectfully recommend that any final rules that are issued with respect to Section 956 not mandate the form of deferral. The agencies should not dictate a "one-size fits all" approach as to the form of deferral and instead should allow each covered institution to establish and implement an appropriate deferral framework given the institution's size and complexity. The agencies should embrace compensation plans and designs such as the EOP and DCCP described above which align our compensation arrangements with those of our investors, rather than implementing rules which could place the continued use of these plans into question. To the extent the agencies retain the requirement that a "substantial portion" of deferred compensation must be in equity-like instruments and deferred cash, we ask that the agencies take into consideration deferred plans such as the EOP and DCCP plans described above and issue final rules that are flexible enough to accommodate such plans in a deferred compensation structure that complies with the Section 956 mandates.

## Conclusion

As explained above, we have participated in various trade group comment letters addressing the Proposed Rulemaking, but we wanted to specifically highlight and comment on the rules which mandate that a substantial portion of deferred compensation be comprised of equity-like instruments and deferred cash. We appreciate the significant efforts the agencies have taken and we hope that our comments are helpful to the agencies' efforts in implementing final rules under Section 956. Please do not hesitate to contact the undersigned if you have any questions regarding our comments or if we can be of any further assistance.

Very truly yours,

/ S / Tom Naratil

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Tom Naratil  
Group Managing Director  
President Americas

/ S / Michael Crowl

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Michael Crowl  
Group Managing Director  
General Counsel Americas

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<sup>5</sup> We note that William C. Dudley, President and Chief Executive Officer of the Federal Reserve Bank of New York, in remarks on October 20, 2014 at the Workshop on Reforming Culture and Behavior in the Financial Services Industry, Federal Reserve Bank of New York, New York City (available at <https://www.newyorkfed.org/newsevents/speeches/2014/dud141020a.html>) promoted awarding deferred compensation in the form of debt instruments.