ZIONS BANCORPORATION

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Via E-Mail

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Re: Incentive-based Compensation Arrangements (the Proposed Rule): OCC 12 CFR Part 42, Docket no. OCC-20111-0001, RIN 1557-AD39; FRB 12 CFR Part 236, Docket No. R-1536, RIN 7100 AE-50;[1]

Ladies and Gentlemen:

Zions Bancorporation (Zions) appreciates the opportunity to comment on the new Proposed Rule on Incentive-based Compensation Arrangements (the Proposed Rule) published by the Board of Governors of the Federal Reserve System (FRB), the Office of the Comptroller of the Currency (OCC), and four other financial industry regulatory agencies (we will refer to the OCC and the other agencies as the Agencies).

Who We Are. Zions is a $59 billion bank holding company with one single chartered national bank, headquartered in Salt Lake City, Utah with bank branches in 11 Western states. We consider ourselves to be a "Collection of Great Banks," with a particular focus on serving small and mid-sized businesses and municipalities throughout the West. Virtually all of our banking activities are very traditional in nature, operated under a straightforward business model that is highly focused on taking deposits, making loans, and providing our customers with a high degree of service. We are primarily a commercial lender, which is to say that we are especially focused on lending to businesses. Notably, roughly half of our total commercial loan commitments consist of loans less than $5 million in size, underscoring our focus on serving smaller businesses throughout the West.

We Commend Constructive, Interactive Implementation of Dodd-Frank Act. Since the 2008 financial crisis and the enactment of the Dodd-Frank Act in 2010, we have worked hard to implement the reforms and improvements in bank management and financial system oversight contemplated by the Dodd-Frank Act, including those recommended in the Guidance on Sound Incentive Compensation Policies issued in 2010 and a notice of Proposed Rulemaking to implement section 956 (Section 956) of the Dodd-Frank Act issued in 2010 (collectively, the Existing Guidance).

Within the context of rulemaking, in the past, we have appreciated the receptiveness of regulatory agencies to industry comments, which has enabled final rules to be implemented in a manner that will

[1] Terms used in this letter that are defined in the Proposed Rule are used with reference to those definitions.

enable achievement of the objectives of the Dodd-Frank Act, some flexibility in application to the widely varying institutions subject to the rules and evolution of the implementation of the rules over time.

A good example of this constructive rulemaking process was the OCC's proposal, modification, and final adoption of its guidelines establishing Heightened Standards for Certain Large Insured National Banks, Insured Federal Savings Associations, and Insured Federal Branches (the Heightened Risk Management Guidance). That proposal contained basic risk management principles and organizational requirements that the industry was, in general, highly supportive of and had already implemented to a very large degree. The proposed Heightened Risk Management Guidance was, however, highly prescriptive, reflecting a "one-size-fits-all" approach, and would have been unnecessarily onerous and inflexible as proposed. The OCC considered industry comments constructively and issued a final rule that we believe fully satisfied the Dodd-Frank Act's objective of heightened risk management, in a principles-based manner that facilitates risk management structures tailored for particular institutions.

We are fully supportive of the principle of designing compensation programs so as to ensure that they do not incentivize inappropriate risk-taking. We are also supportive of particular practices, such as deferral of portions of incentive compensation and the integration of risk-balancing features into the design of incentive plans to facilitate effective risk mitigation. In fact, Zions has already implemented those principles and other practices as well as extensive incentive compensation governance and oversight activities to enforce accountability for adverse risk outcomes.

We believe that the prescriptive, one-size-fits-all approach set forth in the Proposed Rule is not in line with the core objective of Section 956 of the Dodd-Frank Act, which is to prohibit incentive-based compensation practices that encourage inappropriate risks, that are excessive or that could lead to material financial loss. Further, we believe that a risk- and principles-based approach to incentive compensation, similar to the approach taken in the Existing Guidance, will provide institutions across the industry the flexibility to tailor their compensation programs to the specific risks underlying the roles within their business lines.

Principal Concerns While our concerns with the Proposed Rule are many and varied, we would like to focus our comments in this letter on a specific number of key concerns, as described below. We also have provided input to, and generally support the positions taken in, the comment letter filed by the Financial Services Roundtable.

1. Our overriding concern with the Proposed Rule is that we believe it far too prescriptive and is likely to create burdens, complications, competitive issues and other unintended consequences. We do not believe the Proposed Rule's prescriptive approach furthers achievement of the objectives of Section 956 to a significant degree, beyond what has already been accomplished by the Existing Guidance – certainly not to a degree that would justify the burdens and costs. Were the Proposed Rule modified into a more flexible, principles-based regulation, similar to the approach taken in the Existing Guidance, we believe that most of our other concerns would largely disappear or at least would be substantially reduced and lessen the potential for unintended outcomes.
2. By our estimation, the Proposed Rule would create extremely heavy and costly administrative burdens, particularly on Level 1 and Level 2 covered institutions. We think these burdens are largely attributable to the following features of the Proposed Rule:
    - Overly prescriptive and broad definition of Covered Persons, which, covers any employee receiving ***any*** incentive compensation without regard to whether they are material risk-takers. We believe this definition is likely to expand application of the Proposed Rule's basic requirements beyond significant risk takers (SRTs) and senior executive officers (SEOs) to the vast majority of our workforce, including such employees as tellers, loan

processors, and administrative assistants. Such an expansion would cover employees whose activities do not have the capacity to create material risks.

- Overly prescriptive definition of SRTs, which is based on alternative relative compensation and capital exposure tests. These two exacting tests would cover potentially hundreds or thousands of employees (depending on the applicable institution) who are not significant risk takers and who do not have a material impact on the safety and soundness of the applicable institution. Institutions would be forced to apply the Proposed Rules prescriptive requirements across potentially scores of different incentive plans with overlapping performance and vesting periods, which would require institutions to create, at an enormous cost, a highly complex administrative structure to manage an enormously difficult task that exposes the organization to the constant risk of inadvertent regulatory violations, as employees from year to year cycle in and out of the Proposed Rule's prescriptive enhanced compensation structuring rules.

  For Zions, we will likely be forced to apply the Proposed Rule's requirements to an even broader group in light of the need to maintain parity among employees and in order to reduce administrative complexity and expense.
- Unnecessarily detailed and sometimes redundant control requirements under Sections 236.9–236.11, which would require an exponential expansion of compensation risk functions that would outweigh any benefits derived from adoption of the Proposed Rule.

3. As the smallest Level 2 institution that would be covered by the Proposed Rule, we are extremely concerned about the competitive inequities that will almost certainly be caused by the rule. Our best employees will become recruitment targets of larger Level 1 and 2 institutions, as well as smaller Level 3 community banks and credit unions, who will be able to offer our SRTs and SEOs compensation packages free of the deferral and other enhanced compensation structuring requirements contained in the Proposed Rule. Ironically, in an age of concern about "too-big-to-fail" banks, the Agencies are delivering to just such banks an important competitive advantage over "Main Street" and regional banks like us.
4. We are concerned about possible adverse accounting and tax implications that could arise under the Proposed Rule. We do not believe these issues have been adequately evaluated, which could result in unforeseen adverse consequences, as was the case with the poorly considered adoption of the covered fund provisions of the Volcker Rule.

General Considerations

Prior to commenting on particular provisions of the Proposed Rule, we think it may be helpful to make some general points with respect to the Proposed Rule, which underlie our comments later regarding specific provisions.

1. Continue Approach Used in Existing Guidance and FRB Review. We believe the approach taken in the Existing Guidance, which is a more flexible, risk- and principles-based approach, is superior to the prescriptive, one-size-fits-all approach of the Proposed Rule. We do not understand why the Agencies believed it is preferable to require adherence to the highly prescriptive and inflexible provisions of the Proposed Rule, as opposed to a more flexible, principles-based approach. In 2011, the FRB published a report summarizing the results of their extensive review of the incentive compensation practices at 25 large banking organizations (the FRB Review).[2] The FRB review concluded that "all firms . . . have implemented new practices to balance risk and financial results in a manner that does not encourage

[2] Incentive Compensation Practices: A Report on the Horizontal Review of Practices at Large Banking Organizations, October 2011

employees to expose their organizations to imprudent risks".[3] While the FRB noted that there was "further work to do," we believe it is entirely fair to say that the FRB review did not identify any specific shortcomings in the Existing Guidance's approach to implementing Section 956 or any resistance to or evasion of the Existing Guidance on the part of the banking industry.

Very much worth noting, the FRB Review certainly appears to have been supportive of a flexible approach that allowed banking firms to develop risk-sensitive incentive compensation arrangements that were tied to the particularities of the firms' risk profiles, business lines and business models:

> "[T]he use of any single, ***formulaic approach*** to incentive compensation by banking organizations or supervisors ***is unlikely to be effective*** at addressing all incentives to take imprudent risks. . . . The interagency guidance helps avoid the potential hazards or unintended consequences that would be associated with rigid, one-size-fits-all supervisory limits or formulas."[4]

The FRB Review was an extensive, thoughtful analysis of the status of Section 956 implementation, which has not been contradicted by other regulatory findings. We believe the Proposed Rule should be modified throughout to adopt the principles-based approach used in the Existing Guidance and advocated by the FRB review.

2. Recognize Relationship Between Improved Management of Primary Risks and Management of Incentive Compensation Risks. Although incentivizing inappropriate risk-taking through poorly designed compensation is an absolutely valid concern, we believe it is, when viewed with perspective, a relatively minor risk compared to the risk of inadequate management of basic, primary risks, such as credit and market risks. Since the enactment of the Dodd-Frank Act, the risks Section 956 seeks to mitigate through better designed compensation practices have been greatly mitigated by the implementation of the Act's provisions aimed at primary risks, such as the requirements for enhanced risk management and a dynamic, stress test-based approach to capital requirements.[5] We find it disappointing that the Proposed Rule and accompanying commentary virtually ignores this important relationship between the management of basic, primary risks and the management of secondary compensation risks (a relationship the significance

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[3] See FRB Review at 7. Also see the following conclusions: "every firm has made progress", the firms had "implemented new practices to make employees' compensation sensitive to risk" and they had all "changed risk management processes and internal controls to reinforce and support . . . balanced incentive compensation arrangements". See FRB Review, 6-7.

[4] FRB Review, 6 (emphasis added). This conclusion was based on the following observations:

> ***"A key premise … is that the methods used to achieve appropriately risk-sensitive incentive compensation arrangements likely will different across and within firms. Employees' activities and the risks associated with those activities vary significantly across banking organizations and potentially across employees within a particular banking organization. Differences across firms may be based on their principal chosen lines of business and the characteristics of the markets in which they operate, among other factors, affecting both the types of risk faced by the firm and the time horizon of those risks. Even within firms, employees' activities and the attendant risks can depend on many different variables, including the specific sales targets or business strategies and the nature and degree of control or influence that different employees may have over risk taking. … Methods for achieving balanced incentive compensation arrangements at one organization may not be effective at another organization, in part because of the importance of integrating incentive compensation arrangements with the firm's own risk-management systems and business model. Similarly, the effectiveness of methods is likely to differ across business lines and units within a large banking organization."***

FRB Review, 6-7 (emphasis added). We note that the distinctions between Level 1, 2 and 3 Covered Institutions and the variations in the deferral and other requirements applicable can still fairly be considered "formulaic", "one-size-fits-all" and "rigid", inasmuch as these are arbitrary and relatively small variations, not supported by empirical connections between the variations and efficacy of risk mitigation or any other meaningful basis.

[5] For example, it is obvious that the need for constrained incentive compensation arrangements for mortgage and acquisition and development lending would be infinitely more important for a pre-Dodd Frank Act organization without adequate risk and concentration limits than for a post-Dodd Frank Act organization operating within a well-managed risk management structure with risk limits tied to capital and thoughtful risk appetites.

of which was recognized in the FRB Review).[6] We believe the Proposed Rule's prescriptive approach endorses and encourages mechanistic, rules-based incentive compensation arrangements without any reference to the particular business models and risk profiles of different institutions. In our view, the flexible principles-based approach favored by the Existing Guidance and found acceptable by the FRB Review would lead to incentive compensation practices that are far more effective, by fostering a better and more flexible tie between the management of each organization's particular business risks and its incentive compensation practices.

3. Recognize Diversity of Banking Organizations, Incentive Compensation Vehicles, and Complexity of Accounting and Tax Rules. The Proposed Rule exhibits very little sensitivity to the great diversity and complexity of banking organizations and types of compensation arrangements that would be covered by the rule.

In terms of institutions, the Proposed Rule would regulate the incentive compensation programs of very large financial institutions (e.g., Citigroup, JP Morgan, Wells Fargo, etc.) and Zions under an essentially identical regime, notwithstanding that the businesses and risks of these companies have virtually nothing in common. For instance, one large financial institution had annual revenues of $33.8 billion and average total annual compensation ***per employee*** of $345 thousand (including benefit costs) and is one of the most influential participants with respect to many of the largest and most sophisticated underwriting, trading, advisory, derivative and structured vehicle transactions in the world. These business lines were relatively lightly regulated and supervised prior to the financial crisis. It operates in a segment of the banking industry—investment banking—that traditionally utilized incentive compensation practices that paid out large, by comparative standards, annual bonuses based on the amount of revenues produced by employees on an annual basis. Zions has annual revenues of $2.2 billion[7] and average total annual compensation per employee of $95 thousand (including benefit costs).[8] Less than 1% of our employees have total annual compensation in excess of the ***average*** total annual compensation for this large financial organization. Further illustrating the disparity in pay practices between our organization and those in the investment banking industry, we note that the CEO of this large financial institution was awarded more incentive compensation in 2015 than the ***aggregate total*** of incentive compensation granted to all 18 of our highest paid executives for the same performance period.

We engage almost entirely in standard loan and deposit transactions, wealth advisory and investment activities with small and medium-sized businesses and municipalities and individuals. Zions employees are, by comparison, more moderately compensated and provide the ordinary banking services typically associated with community and Main Street banks, the risks of which are relatively well understood and have long been subject to regulatory oversight. The historic compensation programs applicable to a large percentage of our executives were and are structured so that a large percentage of overall and incentive compensation (e.g., approximately 50%) was subject to three-year or longer performance, deferral or vesting periods. Because of this, the introduction of section 956 and the Existing Guidance did not require a substantial reworking of our incentive plans. Rather they mainly required a refinement of provisions, the expansion of risk balancing features to incentive plans for employees further down in our organization and the build-out of oversight and control functions.

We, like other banking organizations that would be covered by the Proposed Rule, employ a large number of incentive compensation vehicles and practices across our organization. These include annual bonuses

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[6] See, e.g., FRB Review, 10 ("Methods for achieving balanced incentive compensation arrangements [may differ] because of the importance of integrating incentive compensation arrangements with the firm's own risk-management system and business model.")

[7] Zions Bancorporation, 10-K filed February 19, 2016, page 37

[8] Zions Bancorporation, 10-K filed February 19, 2016, pages 37-38. Computation is total salary and benefit costs divided by total number of employees

(based on individual, departmental and/or enterprise-wide performance), different types of equity awards, multi-year performance plans, commissions, campaign awards, spot bonuses for extraordinary actions, retention awards and change-in-control arrangements. Many of these vehicles are substantially similar across the industry but are designed with small but significant differences that result in varying accounting and tax ramifications. For example, Zions has employed cash-settled restricted stock units, stock-settled restricted stock units and restricted stock grants, all of which achieve the same basic compensation results—the employee benefits or is hurt by changes in our stock price—but are treated differently for tax and accounting purposes.

The problem with ignoring this diversity is that of any rigid, "one-size-fits-all" approach to addressing a complex issue. First, such an approach may turn out to be appropriate for some institutions and pay practices but less appropriate for others. For example, a solution to a problematic practice used by an institution in one segment of the banking industry—hypothetically, the payment of annual bonuses based on annual production without downward adjustment for deferred amounts—might call for a solution like the Proposed Rule's exact requirements for deferral percentages per award and specific triggers for downward adjustment, but could very well only create unnecessary and disruptive changes in compensation practices and employee cash-flows for another institution that had already implemented incentive compensation practices generally in line with the Existing Guidance and the deferral and downward adjustment provisions of the Proposed Rule.

Second, it is likely that the changes required by the enhanced compensation structuring rules will have unforeseen adverse impacts. For example, the deferral and downward adjustment rules applicable to cash bonuses could result in the recognition of income by employees prior to their receipt of the cash payout. Furthermore, the requirement that approximately half of cash bonuses, as well as approximately half of equity awards, must be deferred will substantially reduce employees' annual cash and other available compensation to satisfy the related tax liabilities.

Third, it is likely that uncertainty about the interpretation and proper application of strict rules will hinder banking organizations from addressing many ad hoc and innocuous employee issues. For example, if an employee receives slightly less than 33% of his or her compensation in the form of incentive compensation, the utility of offering a spot award for detecting and reporting problematic risk issues, which would put the employee into the enhanced compensation structuring regime in the future, might be defeated by the burden that would be placed on the employee's cash flow in the future.

We believe the best way for the Agencies to avoid the unnecessary burdens and unintended consequences of a rigid approach to a complex issue is to modify the Proposed Rule so that it is less prescriptive, enables customization for different organizations based on their risk characteristics and encourages the interpretation and application of Section 956-based principles on a supervisory, rather than cumbersome rulemaking, basis.

Specific Suggestions

1. Use Principles-Based Approach Rather Than Inflexible Prescriptive Requirements. The general principles and approaches contained in the Proposed Rule, including the concepts underlying the rule's provisions regarding such things as performance periods, deferrals, clawbacks, leverage, and other structural compensation factors, appear to be generally consistent with current compensation practices utilized at the top levels of financial institutions with more than $50 billion in total assets. The general principles reflect prudent approaches to the design of incentive compensation programs. Unfortunately, the Proposed Rule is not drafted in terms of general approaches and principles, but has specific prescriptive requirements that apply across an entire institution without regard to that institution's business lines and the risk profiles of those business lines. It is this highly prescriptive approach that gives rise to almost all of our concerns about the Proposed Rule. For example, according to the Existing Guidance, individual banking institutions are required to identify material inherent risk takers and designate them as "covered persons." However, each institution is allowed to determine the method by which it does so, based on the institution's business model and risks. The institution's supervisory authorities are able to assess the appropriateness and effectiveness of the institution's methodology and to require modifications. The supervisors have, in fact, provided informal guidance on many issues, including the rough percentage of the workforce expected to be designated as "covered persons." The current approach combines insights from the regulated entity, whose management best knows the entity's business risks, and insights from the supervisory authorities, who are well placed to assess the entity's place within the banking industry as a whole. This approach seems to be working satisfactorily. If, contrary to the conclusions of the FRB Review, the Agencies do not believe the current approach is functioning satisfactorily, we believe they should detail the shortcomings and explain why strict numeric tests are necessary and how a prescriptive approach will make implementation of Section 956's objectives more effective.

If the Proposed Rule were to be modified and redrafted in a principles-based manner allowing flexibility, even with some numeric guidance, we believe the unnecessary and objectionable negative impacts of the Proposed Rule would be largely reduced or eliminated. For example, the "covered person" identification and designation requirement could be redrafted to state that banking organizations must develop an acceptable, auditable methodology for determining material inherent risk takers, that such methodology should be based on compensation, credit approval or other transactional levels, credit authorities or similar criteria, and that the methodology should generally result in a percentage of the workforce (e.g., 10% to 25%) being subject to incentive compensation structuring principles. Likewise, the enhanced compensation structuring rules would be much more manageable and, we believe, at least equally effective if they were drawn up in a more flexible manner than as currently presented under the Proposed Rule. The burdens and complexities that the Proposed Rule would unnecessarily engender would be greatly reduced by transforming strict numeric requirements into general guidance and allowing aspects of the enhanced compensation structuring rules—such as deferral and downward adjustment of portions of incentive compensation, the length of performance and deferral periods, and the use of quantitative and qualitative factors—to be met on an aggregate rather than per award basis.

We would also recommend that the wording of certain provisions that relate to statutory requirements or plan design, including the definitions of "material financial loss" and "performance measures" be reworded so that inconsistency with the expressed expectation does not ***necessarily*** result in a violation of the statute or design requirement, as is presently the case,[9] but rather provides that a supervisory authority ***"may find"*** that a violation exists. This would provide supervisors greater flexibility in determining whether particular circumstances constitute a "violation of law".

In the comments below, we identify a number of provisions in the Proposed Rule that we believe would be especially problematic across the industry, without an appreciable improvement in risk balancing. We believe the best way of addressing these problematic provisions would be to revise and redraft the Proposed Rule in a principles-based manner. Most of the comments below are intended to demonstrate the practical difficulties with the Proposed Rule as drafted.

2. Modify Approach to Defining Covered Institutions and Rules Applicable to Different Covered Institutions. We believe the Proposed Rule should be modified to apply to all covered financial institutions in a principles-based manner in which the degree of regulatory expectations could be tailored for institutions based on factors tied to institutional and systemic risk. Factors could include such things as the inherent risks of different business activities, the potential impact of an institution's adverse risk

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[9] Such provisions in the Proposed Rules are worded categorically to say a banking organization's compensation arrangement violates the statute or regulation unless it meets the Proposed Rules prescriptive provision.

outcomes on markets and economies and the size or role of an institution's activities in various markets. We are sure the Agencies have already identified factors that raise concerns about systemic and individual institution risk that could be used by supervisors to determine the level of incentive compensation controls appropriate for various types of banking organizations. We believe the arbitrary lines between institutions with assets of less than $50 billion and those equal to or greater than $250 billion, or in between, are so arbitrary as to be ineffective as indicators of inherent risk. We would further note that many members of Congress have suggested that the use of such asset thresholds, without taking into consideration other risk factors such as complexity and interconnectedness, are inappropriate measures of overall risk. If the Agencies feel compelled to base differentiation in the incentive compensation standards applicable to different institutions on asset size alone, the Agencies should provide for much more gradation in levels—perhaps, different levels for every $100 million of assets above $1 billion—as well as the extensiveness of the covered person, SRT, and SEO definitions and enhanced compensation structuring rules applicable to the more finely graded levels. This would, however, add a great deal more complexity to the rule if a prescriptive approach were maintained.

3. Reduce Excessive Scope of Covered Employees. The expanded definition of covered status from an "employee (or group of employees) that exposes the organization to ***material inherent risk***" under the existing guidance to "any employee that receives incentive compensation" under the Proposed Rule's definition of a "covered person" is too broad and would result in unnecessary and overly burdensome administrative efforts. The Proposed Rule's expansion of the "covered person" definition to cover all employees receiving any incentive compensation yields little, if any, risk mitigation benefit because the newly designated "covered persons" will, in all likelihood, be employees that do not have the ability to expose Zions to material inherent risk. Indeed, we are certain that will be the case for Zions, as we have for half a decade undergone a process of identifying employees whose activities expose us to material risk and have implemented risk balancing features into their incentive compensation arrangements.

Zions believes the application of the Proposed Rule to our workforce under our current compensation arrangements would result in grossly excessive coverage. Specifically, applying the current "material inherent risk taker" standard during each of Zions' "covered person" identification and designation reviews, which have been conducted annually since 2011, has resulted in 13–15% of our employee population being designated as "covered persons." Under the new standard promulgated under the Proposed Rule's dramatically expanded definition of "any employee receiving incentive compensation," we project that Zions covered person population ***will likely increase to over 90% of our workforce***. Included in the newly designated covered person population at Zions would be part-time tellers who make as little as $10.50 per hour and who are eligible for and are often paid $10 bonuses for referring customers to associates who are able to complete the sale of new checking or deposit accounts. It seems improbable that the Agencies truly intended to have financial institutions subject all incentive compensation awards to the same level of extensive underlying governance, risk management oversight and recordkeeping requirements currently being applied to incentives paid to employees who have been identified under the Existing Guidance as having the capacity to expose the organization to material inherent risks. These activities would include, but not be limited to, the review and documentation of the incentive plan, documentation of each incentive compensation decision, periodic modeling and backtesting of incentive plan results, and a multiyear recordkeeping and reporting requirement.

The cost of implementing suitable incentive governance and oversight controls for this exponential increase in the number of covered persons would be enormous and far outweigh any benefits of adoption of the proposal. For example, we estimate that we would need to prepare, collect, and review more than 50,000 pages of documentation annually simply to comply with the oversight and recordkeeping requirements for one of our incentive plans, which covers approximately 35% of our workforce.[10] Given

[10] This estimate is based on the documentation we produced in response to a regulatory request for a sampling of 33 persons involved in the plan, which covers approximately 3,500 employees. For the 33 persons, we provided 800 pages, or 24 pages

that we have multiple incentive plans and believe the Proposed Rule will extend to a much greater percentage of our workforce, we think our concern about the administrative burdens of the rule is well justified. Because of the high cost and administrative burdens of the Proposed Rule's expansive scope, we believe the definition for covered persons should not be expanded as proposed but should continue to rely on the previous standard of "material inherent risk-takers." Also, we believe that the Agencies should consider implementing a *di minimus* incentive compensation amount (e.g., $100,000 or less) that would exempt employees from the "covered person" designation to help alleviate the degree of the potential unnecessary administrative burden.

4. ***Eliminate the Exposure Test.*** The exposure test described under the Proposed Rule is deeply flawed conceptually, would require substantial changes in risk practices and administrative systems, would expose covered institutions to significant competitive harm, and should be eliminated. The exposure test would define an SRT—who would be subject to the Proposed Rule's enhanced restrictions—in part as an employee who had the ability to expose 0.5% of a covered institution's capital to risk over time.

We believe the design of the exposure test is faulty on several dimensions. First, it utilizes an approach to risk limits that simply is not used by Zions or, to our knowledge, other commercial banks. As noted above, we are a commercial bank whose principal business is making loans. We have virtually no securities or derivative trading activities. Our lending activities are covered by robust and extensive policies and procedures, including overall concentration limits, individual borrower lending limits, and credit and approval policies and practices. These have always been tied in one way or another to the risk to our capital measured on a per-transaction, per-borrower or aggregate loan type basis. Credit authorizations are reviewed annually but have never been granted to employees based on their theoretical ability to expose our capital to loss over a specified time frame (e.g., 12 months), as contemplated by the Proposed Rule. We are not aware that any of our peer financial institutions structure their credit limits to include time-bound restrictions. Additionally, the Proposed Rule's requirement that "a covered person [having] no specific maximum amount of lending for the year....would be assumed to have an authorized annual lending amount in excess of the 0.5% threshold" yields clear unintended consequences. For example, it is implausible that the Agencies intended for this requirement to mandate that branch personnel with minimal overdraft approval authority would potentially become subject to the SRT designation and the related enhanced compensation structuring requirements. This test seems to us to be an example of the mistake of applying a rigid rule to diverse institutions; as such an approach would only create burdens unjustified by any improvement in incentive compensation risk management.

Second, application of this rule to Zions would dramatically increase the number of covered persons within our organization and the population of employees that could become subject to the mandatory enhanced compensation structuring rules associated with the SRT designation. We anticipate that within our organization over 350 employees (or 3.5% of our workforce), including some branch managers and mid-level commercial bankers, earning as little as $100,000 per year in base salary and $160,000 in total compensation, are likely to be designated as SRTs as a result of the exposure test. It is conceivable that Zions could avoid this result by redesigning not only our compensation plans but also our entire credit risk philosophy and structure. For example, we might be incented to devise a credit approval structure in which only high-level executives and high-level credit administration personnel could approve any loans, with lending personnel having no approval authority. Such a wholesale change in the fundamentals of credit risk management would, however, run the risk of unforeseen consequences even if it could be designed and adopted.

Third, the exposure test is very likely to result in competitive harm to all but the largest Level 1 and all of the Level 3 covered institutions. At smaller Level 2 covered institutions the exposure test is likely to

per person. In estimating the burden relative to the whole plan, we reduced the 85,000 page extrapolation on the assumption, that there might be efficiencies associated with the larger scale.

reach a large number of employees, like branch managers and mid-level commercial bankers, whose peers at Level 3 and larger Level 2 and Level 1 institutions will not be reached by the exposure test. The reason for this is that (1) with respect to Level 1 and 2 institutions, that test is based on the size of an institution's capital, which will translate to a smaller dollar-based capital at risk threshold applicable to individual employees and (2) with respect to Level 3 institutions, they are not subject to the test. As a result, it is likely that bankers serving individuals and small- and medium-sized businesses for a large institution, like JP Morgan or Citibank, are unlikely to be subject to the Proposed Rule's enhanced compensation structuring rules, whereas our best bankers serving that segment are likely to be subject to the Proposed Rule's unattractive deferral, clawback and other provisions. This will make our best employees subject to recruiting raids, providing too-big-to-fail banks with an unfair competitive advantage over Main Street banks like us.

For these reasons, we believe the Agencies should discard the proposed exposure test in its entirety. It would require wholesale restructuring of historic approaches to credit risk management, as well as lender compensation. The exposure test ignores the reality that, under current risk management practices, exposure to capital over time is already managed on an overall basis by extensive and varied means connected to risk appetite frameworks and other risk management tools. If a banking organization has satisfactory policies and practices to manage and limit overall risk to capital it is unclear why it should be necessary to implement a capital exposure test to the individual actors who contribute to the managed and limited overall exposures.

5. Discard the Relative Compensation Test. We believe the Proposed Rule's strict relative compensation test should be discarded because its implementation will unnecessarily burden banking organizations and because its precision will make it a blunt tool for supervisory authorities. Supervisory authorities are likely to find that a far larger, or smaller, percentage of a particular banking organization's workforce should be subjected to the Proposed Rule's enhanced compensation structuring requirements.

As with the exposure test, there is a very substantial unfair competitive implication to the relative compensation test. Depending on the size of a banking organization an employee with a particular function—perhaps a branch manager, a lender or a compliance officer—in one institution (for example, a mid-sized institution) may be subject to the Proposed Rule's prescriptive enhanced compensation structuring requirements while an employee with a comparable position in another institution (a larger institution or an institution with total assets under $50 billion) will not be. This will create the very serious risk that the first institution will be vulnerable to raids on its workforce and, particularly its best employees. This would not be a one-time transitional risk, but a constant, interminable situation. The competitive risk could not be mitigated or eliminated through changes to credit or other risk management practices or changes to compensation levels. (The only solution would appear to be a wholesale elimination of incentive compensation of one-third or more of total compensation to employees other than senior executives.)

The Agencies have specifically asked whether the percentage-based relative compensation test should be replaced with a single, set compensation level, such as $1,000,000. As we have explained above, we believe a general, principles-based approach would be far superior to any precise numeric test. If, however, the Agencies believe a precise numeric test is essential, we believe a set dollar amount of compensation would be far better than a percentage-based test. A set threshold applicable to employees of all covered institutions would alleviate the competitive inequities described above. A set dollar threshold would also reduce the administrative burden of identifying a percentage of employees to be designated as SRTs on an annual basis. If a set dollar amount is used we believe a $1,000,000 threshold would be acceptable (though it should be indexed to account for inflation in future years).

6. Combine Performance and Deferral Periods into a Single At-Risk Period. The Proposed Rule creates two time-based categories of incentive awards—short-term awards,[11] having a performance period of less than three years, and long-term awards, having a performance period of three years or more. Applying these classifications to the compensation structure at Zions results in a three-year deferral period for 40–50% of short-term awards and a one-year period for 40–50% of long-term awards, in each case based on whether the employee is an SRT or an SEO. This seems to us to be an example of over-engineering and unnecessary prescriptiveness. As a practical matter, it eliminates the flexibility of banking organizations to utilize performance periods other than one and three years because of the burden it would place on employees. For example, if there were a two-year performance period or a four-year performance period, employees could not fully realize compensation for five years instead of four years from the commencement of the performance period. We are curious about the reasons why the Agencies wish to discourage banking organizations from utilizing performance periods of other than one or three years, particularly inasmuch as the Proposed Rule requires that incentive compensation awards be subject to reduction on the same basis in both performance and deferral periods. It may seem like a small matter to standardize performance periods across the industry, but, there could be many unanticipated reasons why an institution might wish to have flexibility in setting the length of performance periods. Examples would include, among other things, a mid-year reorganization, the timing of mergers, divestitures or acquisitions, or the need to implement vital strategic initiatives.

In light of our general comments, we believe the Proposed Rule should address the distinction between short- and long-term incentive compensation and the deferral of payouts in a less prescriptive manner. If the Agencies believe fixed standards based on defined time periods is necessary, we would recommend that the Proposed Rule be modified so that the combined length of the performance period and deferral period is at least four years and during that period that the award be subject to downward adjustment, non-vesting or forfeiture, as the case may be, on the basis of criteria contained in the Proposed Rule. This would seem to be sufficient to fully achieve the objective of deferring the realization of compensation beyond the end of a specified performance period. It subjects incentive compensation to continued performance over time in order to incentivize care in decision making and to temper short-term financial pressures without concern about longer-term outcomes.

7. Allow Amount of Deferred Incentive Compensation to be Determined on Aggregate Rather Than Per Element Basis. The Proposed Rule requires that set percentages, ranging from 40% to 60%, of each and every incentive compensation award be deferred. This seems to us to be another example of over-engineering and unnecessary prescriptiveness. The point, it would seem, is for a substantial portion—perhaps 40% to 50% in our case—of an executive's incentive compensation be subject to delayed realization so as to incentivize more careful consideration on long-term risk outcomes in business decision-making. We believe this principle would be fully served by requiring that a substantial percentage of ***aggregate*** annual incentive compensation be subject to delayed realization and downward adjustment, rather than the same percentage of ***each and every*** grant or cash award. The difference is that the Proposed Rule's approach limits flexibility in designing compensation programs and the form of payout, without a clear risk mitigation benefit.

The "each and every" approach to deferral may also reduce the ability of banking organizations to utilize special compensation grants for special purposes. For example, it is common to offer employees special incentive awards, such as campaign rewards and spot bonuses (including bonuses and rewards paid to incentivize risk mitigation efforts). The Proposed Rule would by its words appear to require such deferral for SEOs and SRTs. We believe this is another example of the flaw of an overly prescriptive approach to solving complex issues, although requiring deferrals in such circumstances would largely defeat the utility of such tools.

[11] Referred to as "qualifying incentive compensation" for reasons that are not clear.

We would recommend that the Agencies revise the deferral provisions so as to enable them to be implemented in a more flexible manner without fixed timeframes, in conformity with general guidance. If that approach is not acceptable to the Agencies, we recommend that the Proposed Rule be modified so that required deferral percentages may be met in the aggregate, thereby allowing greater flexibility in application while still achieving the objectives of the Proposed Rule.

8. Modify Requirement For Financial and Non-Financial Performance Factors. The Proposed Rule requires that any incentive-based compensation arrangement include both financial and non-financial measures of performance. Literally read, this would mean that the Proposed Rule would be violated if a banking organization awarded a spot bonus as a reward for exceptional performance—for example escalating a material risk issue—because no financial measure would be involved.[12] We are confident that this is not a result the Agencies intended. Two modifications seem like they might be helpful, depending on the Agencies' purpose in including the provision in the Proposed Rule.

First, if the purpose is that, for any incentive-based compensation arrangement involving a performance period, the determination of the award amount must be subject to risk-balancing features that can result in downward adjustments, the Proposed Rule should be modified to say only that (and not include the general mandate that all incentive-based compensation have the two measurement features). This is something that we already broadly do. Alternatively, if the Agencies intended to mandate that all incentive-based compensation have the dual performance measures, we would suggest that the provision be modified to apply on an aggregate basis, so that some incentive arrangements can have only financial or non-financial measures of performance, as long as the compensation plans offered to an employee, taken as a whole, contain a mix of the two measures.

9. Remove or Modify Requirement That All Incentive-Based Compensation Plans Provide For Deferral of Both Cash and Equity-Like Instruments. Literally read, this would seem to require each form of incentive compensation subject to the enhanced compensation structuring rules be deferred in portions of cash and equity. This would, obviously, make no sense in the context of the typical annual cash bonus or the grant of restricted stock. We suggest that, if the requirement is to be maintained, it be worded to say that the employee's overall compensation package provide for deferral of both elements.[13] Having said that, we do not understand the need for this requirement and, particularly, why it must apply to all employees receiving incentive compensation. We have many employees whose compensation is likely to be subject to the structuring rules, but today receive only cash incentive compensation. It is unclear why their status as an SEO or SRT should require that they receive equity.

10. Clarify Distinctions Among Incentive-Based Compensation Arrangement, Plan and Program. The intended purpose of these distinctions is very unclear.

11. Distinguish Between Incentive-Based Compensation and Commissions. Typically, a commission-based employee does not receive a salary, or they receive a modest salary that is really a draw against commissions. At Zions, commissions are sometimes the only compensation that a person receives and often takes the place of a traditional salary. Therefore, deferring compensation at the level suggested by the Proposed Rule would affect commission-based employees more significantly than other employees receiving traditional incentive compensation with a fairly large salary.

[12] There are many other types of incentive payments that typically are not measured both on financial and non-financial bases, including contributions to profit-sharing plans, commission payments and SVA-based performance plans.

[13] Because the Proposed Rule uses the term, "Incentive-Based Compensation Plan" in this context, the Agencies may be assuming that all covered institutions provide comprehensive incentive-based compensation plans, including cash and equity features, to ***all*** employees. Although some institutions may do this, others may use various compensation vehicles for different employees on a more ad hoc basis.

12. Eliminate the Limitations on Volume-Driven Incentive-Based Compensation. Many employees at Zions, who are neither SEOs nor SRTs, have a substantial portion of their compensation that is based on commissions or similar performance. In addition to being overly prescriptive, these limitations are simply unnecessary in light of the Proposed Rule's extensive deferral, forfeiture, downward adjustment, and clawback requirements.

13. Expand the Allowable Circumstances for Accelerated Vesting of Incentive Compensation. The Proposed Rule would only allow accelerated vesting and payout of deferred amounts in the event of the covered person's death or disability. Zions acknowledges that there are complex policy considerations for circumstances under which acceleration of vesting and payment should be permitted. At a minimum, Zions believes that the final rule should allow accelerated vesting and payment of both cash and equity-like awards where a covered person is terminated without cause following a change-in-control. It would not be appropriate for a covered person whose employment was terminated in connection with a change in control to have the value of future vesting of his or her awards tied to a company for which the covered person never worked. The final rule also should allow accelerated vesting and payment of equity-like awards where the acquirer in a change of control fails or refuses to exchange and continue the equity awards.

14. Clarify "Incentive Based Compensation" Definition. The term "incentive-based compensation"—defined as "any variable compensation, fees, or benefits that serve as an incentive or reward for performance"[14]-underlies most of the Proposed Rule's substantive provisions, including those defining covered persons, SRTs and setting forth enhanced compensation structuring requirements. Thus, it will be very difficult for banking organizations to build compliant compensation programs without clearly understanding the meaning of the term. Although compensation professionals have a fairly consistent idea of what is meant when incentive compensation is discussed, the Proposed Rule contains a prescriptive definition of the application which could result in inconsistencies. For example, do spot bonuses, campaign awards, and commissions constitute incentive-based compensation? They all appear to fall literally within the definition, but it is difficult to see how they could comply with the Proposed Rules enhanced compensation structuring requirements. Similarly, does time-vesting restricted stock constitute incentive-based compensation? Compensation professionals would probably treat such stock as incentive compensation because its value can increase prior to vesting as a result of positive performance. Yet, restricted stock could be granted "based solely on the covered person's level of fixed compensation and [in a manner that does] not vary based on one or more performance measures," which the accompanying commentary says would cause compensation not to be treated as incentive-based. If the latter were the correct interpretation, it would appear that the restricted stock grant described above would be transformed into incentive-based compensation if the grant amount were based partly on the employee's performance over a prior period or if vesting were subject to performance criteria. But it is not obvious why these different ways of utilizing restricted stock should be treated differently from a risk management perspective.

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[14] Emphasis added. The difficulty of understanding the term is compounded by the fact the definition is embedded with two important terms having meanings that are difficult to apply, "variable compensation" and "incentive or reward for performance." For example, salary, which the accompanying commentary says is not variable, does vary from year to year and within years, in part based on merit increases, which would in turn be based on performance. And the possibility of merit increases undoubtedly incentivizes employees to perform well. Virtually all compensation and benefits could be seen as falling within this term, as compensation and benefits are why employees perform. Further, the word "performance" is difficult to apply. Does an increase in stock value constitute performance? If so, vesting periods of an equity grant would be considered part of the performance period. If not, why would holding company SVA-based performance plans not also be excluded as they also reflect high level holding company performance?

The point is not to be critical or contentious but to emphasize how intractable the problem of defining incentive-based compensation is likely to be. We believe the best approach would be a general revision of the Proposed Rule in a flexible principles-based manner. This would allow a banking organization and its supervisor to determine what should be considered incentive-based compensation and what should not on a case-by-case basis, taking into consideration the organization's overall compensation program, the manner in which a particular compensation vehicle is used and the materiality, or relative amount, of the compensation vehicle at issue. If the Agencies elect to maintain the Proposed Rule's rigid prescriptive approach, we strongly recommend that they comprehensively review commonly used compensation vehicles and state which are and which are not considered incentive-based compensation; otherwise, banking organizations would be placed in jeopardy of violating the Proposed Rule notwithstanding their best efforts to comply.

15. Reduce the Length of the Clawback Period. The Proposed Rule requires that specific portions of incentive compensation be subject to clawback for a period of seven years from the end of the deferral period. The seven-year period seems excessive to us, as an employee would not be able to enjoy fully his or her incentive compensation without the overhang of possible clawback for at least 11 years. In our experience, reliably and accurately assessing past facts and fairly attributing accountability becomes more challenging as the time period between the event and the assessment lengthens. This will be especially true with respect to clawback issues, the assessment of which will require a careful parsing of facts, actions and clarity of policies and controls; different individuals' roles in decision-making, often in group contexts; the intent and motivation of individuals and their ability to be aware of or to change the direction of risk issues; all of which are often difficult to discern clearly even contemporaneously with the events. These kinds of concerns about aged reconstruction of facts and individual intent have given rise over the centuries to statutes of limitations, which now apply to virtually all legal causes of action. Compared to standard statutes of limitations, the seven-year clawback period is very long. For example, under Utah law, where Zions is incorporated, statutes of limitations are generally two to four years and rarely as long as seven or eight years. Only offenses involving grievous criminal conduct (e.g., murder and arson) are longer than eight years. We would suggest the mandatory clawback period be reduced to a timeframe of no more than three years.

16. Provide for Transition Period After Effective Date. Due to the significantly expanded scope of employees who would become subject to prescriptive enhanced compensation structuring restrictions as a result of the Proposed Rule's SRT definition, a large number of employees would likely face substantial changes in the amount of compensation available to them annually for expenditure or savings. This impact would be alleviated over time, as deferred amounts vested and became available to employees, but would be significant to existing employees upon effectiveness of the Proposed Rule and to new employees as they are hired. If the Proposed Rule is not revised generally to provide more flexibility, we believe modifications to the Proposed Rule's deferral requirements, combining the performance period and deferral period into a single at-risk period and allowing deferral amounts of incentive compensation to be calculated in the aggregate rather than on a per-award basis, would be the best way to address this adverse transitional impact on employees. If the Agencies are unwilling to modify the deferral requirements, however, we would recommend that the Proposed Rule be modified in some manner to allow banking organizations to phase the rule in over time after the Effective Date so as to cushion the impact of compensation design changes on employees.

17. Further Research and Coordination is Needed to Eliminate the Adverse Tax and Accounting Effects Created by the Proposed Rule. Absent specific action by Congress, the Internal Revenue Service, and the Financial Accounting Standards Board, the deferral, forfeiture, downward adjustment, and clawback requirements could have adverse tax and accounting effects on organizations and employees covered by the Proposed Rule. Specifically, the discretionary deferrals, similar to other clawback programs, could lead to more income statement variability as all equity awards may become subject to liability accounting treatment. We are concerned our stock-based awards would no longer qualify for equity classification accounting treatment if the Proposed Rule was adopted in its current form, which would require us to re-measure all such outstanding stock awards at the awards' fair value each reporting period and produce artificial earnings volatility.

18. Lessen Detail and Burdens of Control Requirements. We would ask that the Agencies review Sections 236.9 – 236.11 and revise them to make them less exacting and burdensome. The following are some provisions that merit review

- 236.9(a), which would seem to preclude any first line employee from participating in compensation risk decision-making;
- 236.9(b), which would seem to prevent incentive risk control personnel from participating in any company performance- or equity-based compensation programs and to require both financial and non-financial measures of performance tied to control functions for those whose compensation is subject to the enhanced compensation structuring rules;
- 236.10(b)(i), which requires the risk and audit committees of an institution's board, rather than risk or audit management, to report to the full board on the effectiveness of compensation risk management (even though the committee would be relying on management functions when it reports to the full board);
- 236.10(b)(2), which requires two separate but virtually identical reports ***at least*** annually; and
- 236.11, which has very detailed policy requirements, including, for example, that there be ***substantive*** and ***procedural criteria*** for determining whether an employee's ***death*** or ***disability*** has occurred (the only circumstances that could give rise to acceleration of deferred amounts) (clause d); that the role and identity of each employee authorized to make an incentive compensation decision by catalogued (clause e); and that describes how discretion is to be exercised, which would appear to be an oxymoron (clause e).

19. Clarify Regulatory Pronouncements That Will Govern After Rule Becomes Effective. Finally, it is unclear whether the Existing Guidance will remain effective after the Proposed Rule becomes final. One would think not, because the Existing Guidance envisions a regime based on a proposed rule that would have been superseded. If the Agencies intend that banking organizations be subject to both the Existing Guidance and the Proposed Rule, we would recommend that they carefully consider the difficulty placed on banking organizations having to comply with two very different regulatory structures and provide detailed guidance on how the two structures should be managed as an integrated compliance structure.

In closing, we believe that the requirements of the Proposed Rule will lead to inadvertent adverse consequences that may very well create more systemic risk than they will possibly eliminate. The most talented professionals in the banking industry will, in all likelihood, over time, be drawn to work for hedge funds and other financial organizations not subject to this uninviting framework. Surely, having talented bankers working at our largest insured depository institutions is vital to risk mitigation.

Zions appreciates the opportunity to comment on the Proposed Rule and looks forward to the continued development of these important standards.

Thank you.

Sincerely,

Harris H. Simmons
Chairman & Chief Executive Officer