

**Supporting Statement for the
Recordkeeping Provisions Associated with the
Guidance on Sound Incentive Compensation Policies
(FR 4027; OMB No. 7100-0327)**

Summary

The Board of Governors of the Federal Reserve System (Board), under authority delegated by the Office of Management and Budget (OMB), proposes to extend for three years, without revision, the Recordkeeping Provisions Associated with the Guidance on Sound Incentive Compensation Policies (FR 4027; OMB No. 7100-0327).¹ The Guidance on Sound Incentive Compensation Policies (the Guidance) is an interagency publication that is intended to assist banking organizations in designing and implementing incentive compensation arrangements that do not encourage imprudent risk-taking and that are consistent with the safety and soundness of the organization. The Guidance contains voluntary recordkeeping activities. With respect to organizations regulated by the Board, the voluntary Guidance applies to U.S. bank holding companies, savings and loan holding companies, state member banks, Edge Act and agreement corporations, and the U.S. operations of foreign banks with a branch, agency, or commercial lending company subsidiary in the United States (collectively, banking organizations).

The estimated total annual burden for the FR 4027 is 210,920 hours.

Background and Justification

The Board, along with the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), and the subsequently abolished Office of Thrift Supervision (collectively, the agencies), promulgated the Guidance in 2010. In the *Federal Register* notice² announcing the Guidance, the agencies noted that the financial services industry's incentive compensation practices contributed to the financial crisis that began in 2007. Banking organizations often rewarded employees for increasing the firm's short-term revenue or profit without adequate recognition of the risks the employees' activities posed for the firm. The agencies noted that certain compensation practices can encourage employees at various levels of a banking organization to undertake imprudent risks that adversely affect the risk profile of the firm.

The Guidance aims to help protect the safety and soundness of banking organizations and promote the improvement of incentive compensation practices throughout the banking industry. In addition, the Guidance is consistent with the Principles for Sound Compensation Practices

¹ There is no formal reporting form for this collection of information (the FR 4027 designation is for internal purposes only).

² 75 FR 36395 (June 25, 2010).

adopted by the Financial Stability Board (FSB) in April 2009,³ as well as the Implementation Standards for those principles issued by the FSB in September 2009.⁴

Description of Information Collection

The Guidance is based on three key principles. These principles provide that incentive compensation arrangements at a banking organization should:

1. Provide employees incentives that appropriately balance risk and reward;
2. Be compatible with effective controls and risk-management; and
3. Be supported by strong corporate governance, including active and effective oversight by the organization's board of directors.

The recordkeeping provisions of the Guidance are contained within principle 2 and principle 3.

Compatibility with Effective Controls and Risk Management

Pursuant to Principle 2 of the Guidance, a banking organization's risk-management processes and internal controls should reinforce and support the development and maintenance of balanced incentive compensation arrangements. Principle 2 states that banking organizations should create and maintain sufficient documentation to permit an audit of the organization's processes for establishing, modifying, and monitoring incentive compensation arrangements. Additionally, global systemically important bank holding companies and banking organizations subject to Category II-IV enhanced prudential standards under Regulation YY and foreign banking organizations required to form an intermediate holding company under Regulation YY should maintain policies and procedures that (1) identify and describe the role(s) of the personnel, business units, and control units authorized to be involved in the design, implementation, and monitoring of incentive compensation arrangements, (2) identify the source of significant risk-related inputs into these processes and establish appropriate controls governing the development and approval of these inputs to help ensure their integrity, and (3) identify the individual(s) and control unit(s) whose approval is necessary for the establishment of new incentive compensation arrangements or modification of existing arrangements.

Strong Corporate Governance

Pursuant to Principle 3 of the Guidance, banking organizations should have strong and effective corporate governance to help ensure sound compensation practices. The Guidance states that a banking organization's board of directors should approve and document any material exceptions or adjustments to the organization's incentive compensation arrangements established for senior executives.

³ See FSB Principles for Sound Compensation Practices (April 2, 2009), available at https://www.fsb.org/wp-content/uploads/r_0904b.pdf.

⁴ See FSB Principles for Sound Compensation Practices: Implementation Standards (September 25, 2009), available at https://www.fsb.org/wp-content/uploads/r_090925c.pdf.

Respondent Panel

The FR 4027 panel comprises banking organizations, as defined above.

Time Schedule for Information Collection

The recordkeeping provisions in the Guidance are ongoing. The documentation associated with the Guidance is maintained by each institution; therefore, it is not collected or published by the Federal Reserve System.

Public Availability of Data

The documentation set forth in the guidance is a recordkeeping provision, and no data related to this information collection is made available to the public by the Federal Reserve.

Legal Status

The recordkeeping provisions of the Guidance are authorized pursuant to the Board's examination and reporting authorities, located in sections 9, 11(a), 25, and 25A of the Federal Reserve Act,⁵ section 5 of the Bank Holding Company Act,⁶ section 10(b) of the Home Owners' Loan Act,⁷ and section 7(c) of the International Banking Act,⁸ and by section 39 of the Federal Deposit Insurance Act, which authorizes the Board to prescribe compensation standards.⁹

Because the recordkeeping provisions are contained within guidance, which is nonbinding, they are voluntary.¹⁰ There are no reporting forms associated with this information collection.

Because the incentive compensation records would be maintained at each banking organization, the Freedom of Information Act (FOIA) would only be implicated if the Board obtained such records as part of the examination or supervision of a banking organization. In the event the records are obtained by the Board as part of an examination or supervision of a banking organization, this information is considered confidential pursuant to exemption 8 of the FOIA, which protects information contained in "examination, operating, or condition reports" obtained in the bank supervisory process.¹¹ In addition, the information may also constitute nonpublic commercial or financial information, which is both customarily and actually treated as private by the respondent, and thus may be kept confidential by the Board pursuant to exemption 4 of the FOIA.¹²

⁵ 12 U.S.C. §§ 325, 248(a), 602, and 625.

⁶ 12 U.S.C. § 1844.

⁷ 12 U.S.C. § 1467a(b).

⁸ 12 U.S.C. § 3105(c).

⁹ 12 U.S.C. § 1831p-1(c).

¹⁰ See 12 CFR 262.7.

¹¹ 5 U.S.C. § 552(b)(8).

¹² 5 U.S.C. § 552(b)(4).

Consultation Outside the Agency

The Board has consulted with the FDIC and OCC and confirmed that there will be no revisions to the guidance.

Public Comments

On September 1, 2021, the Board published an initial notice in the *Federal Register* (86 FR 49033) requesting public comment for 60 days on the extension, without revision, of the FR 4027. The comment period for this notice will expire on November 1, 2021.

Estimate of Respondent Burden

As shown in the table below, the estimated total annual burden for the FR 4027 is 210,920 hours. The Board estimates that respondents would take, on average, 40 hours each year to maintain policies and procedures to monitor incentive compensation arrangements. The Board also estimates that, in the case of a new institution becoming subject to the guidance, it would take 480 hours each year for large institutions and 80 hours each year for small institutions. These recordkeeping provisions represent 2.35 percent of the Board's total paperwork burden.

FR 4027	Estimated number of respondents ¹³	Annual frequency	Estimated average hours per response	Estimated annual burden hours
One-time Implementation:				
Large institutions	1	1	480	480
Small institutions	1	1	80	80
Ongoing maintenance	5,259	1	40	<u>210,360</u>
<i>Total</i>				210,920

The estimated total annual cost to the public for this information collection is \$12,475,918.¹⁴

Sensitive Questions

¹³ Of these respondents, 3,629 are considered small entities as defined by the Small Business Administration (i.e., entities with less than \$600 million in total assets), www.sba.gov/document/support--table-size-standards.

¹⁴ Total cost to the public was estimated using the following formula: percent of staff time, multiplied by annual burden hours, multiplied by hourly rates (30% Office & Administrative Support at \$20, 45% Financial Managers at \$73, 15% Lawyers at \$72, and 10% Chief Executives at \$95). Hourly rates for each occupational group are the (rounded) mean hourly wages from the Bureau of Labor and Statistics (BLS), Occupational Employment and Wages, May 2020, published March 31, 2021, <https://www.bls.gov/news.release/ocwage.t01.htm#>. Occupations are defined using the BLS Standard Occupational Classification System, www.bls.gov/soc/.

This collection of information contains no questions of a sensitive nature, as defined by OMB guidelines.

Estimate of Cost to the Federal Reserve System

Since records are maintained at the banking organization, the estimated cost to the Federal Reserve System is negligible.