Statement by Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
Notice of Proposed Rulemaking on Incentive-Based Compensation Arrangements
April 26, 2016

Overview of Section 956

Section 956 of the Dodd Frank Act addresses an important lesson from the financial crisis: poorly designed financial institution compensation programs can provide incentives for short-term risk taking that can jeopardize the safety and soundness of the institution.

Material Loss Reviews of failed institutions issued by the inspectors general for the three federal banking agencies found that, in a number of instances, poor compensation practices were a contributing factor to the institution's failure. When poor compensation practices involve the largest financial institutions, the negative impacts of inappropriate risk-taking can have broader consequences for the financial system.

The statute requires six agencies -- the FDIC, OCC, Federal Reserve Board, NCUA, SEC, and FHFA -- to jointly issue regulations or guidelines that prohibit incentive-based compensation arrangements that encourage inappropriate risks by covered financial institutions with assets of $1 billion or more:

- by providing an executive officer, employee, director, or principal shareholder with excessive compensation, fees, or benefits; or
- that could lead to material financial loss at the institution.

Covered financial institutions are also required to disclose to the appropriate federal regulator the structure of incentive-based compensation arrangements.

Overview of the Proposed Rule

Today, the FDIC Board is considering a proposed rule to implement Section 956. The proposed rule seeks to align employee incentives with the long-term interests and safety and soundness of covered financial institutions. As staff described, the proposal uses a tiered approach with three size categories of covered institutions: Level 1, with $250 billion or more in total assets; Level 2, with $50 to $250 billion; and Level 3, with $1 to $50 billion.

All covered institutions would be subject to a basic set of requirements and prohibitions, and more stringent provisions would apply to the two categories of larger institutions. Staff has described the details of the basic provisions.

In regard to the larger institutions, this proposal would require minimum deferral amounts and time periods for incentive-based compensation arrangements for senior executive officers and other employees who can expose the institution to material levels of risk, known as significant risk-takers. The proposal also requires those deferred amounts to be subject to forfeiture and downward adjustment, in the event of undue risk taking as defined in the firm's program and other factors as described by staff. Deferral provides an important mechanism to discourage inappropriate risk-taking by allowing time to pass to evaluate the outcomes of risk-taking behavior and to adjust incentive-based compensation accordingly.

Conclusion

The proposal seeks comment on all aspects of the rule through July 22, 2016. This is perhaps the most important Dodd-Frank rulemaking remaining to be implemented. I support the proposed rule. We look forward to expeditiously reviewing the comments received and moving forward with a final rule. Let me conclude by thanking the FDIC staff as well as the staff of the other agencies for their dedication and commitment to completing this proposed rulemaking.