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FDIC Board Approves for Public Comment Interagency Rule to Implement the Incentive-Based Compensation Requirement Under Dodd-Frank Reform Act

The Board of Directors of the Federal Deposit Insurance Corporation (FDIC) today approved a joint proposed rulemaking to implement Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Section 956 prohibits incentive-based compensation arrangements that encourage inappropriate risk taking by covered financial institutions and are deemed to be excessive, or that may lead to material losses.

Consistent with Dodd-Frank, the proposed rule does not apply to banks with total consolidated assets of less than $1 billion, and contains heightened standards for institutions with $50 billion or more in total consolidated assets. For these larger institutions, the rule requires that at least 50 percent of incentive-based payments be deferred for a minimum of three years for designated executives. Moreover, boards of directors of these larger institutions must identify employees who individually have the ability to expose the institution to substantial risk, and must determine that the incentive compensation for these employees appropriately balances risk and rewards according to enumerated standards.

Chairman Bair said "This proposed rule will help address a key safety and soundness issue which contributed to the recent financial crisis – that poorly designed compensation structures can misalign incentives and induce excessive risk-taking within financial organizations. Importantly, we believe the rule will accomplish its objectives in a way that appropriately reflects the size and complexity of individual institutions. Importantly, this inter-agency proposal will apply across all types of US financial institutions, limiting the opportunity for regulatory arbitrage. Similarly, it will better align US compensation standards with those which have been adopted internationally under the framework approved by the Financial Stability Board in 2009. "

The proposed rule would move the U.S. closer to aspects of international compensation standards by 1) requiring deferral of a substantial portion of incentive compensation for executive officers of particularly large institutions described above; 2) prohibiting incentive-based compensation arrangements for covered persons that would encourage inappropriate risks by providing excessive compensation; 3) prohibiting incentive-based compensation arrangements for covered persons that would expose the institution to inappropriate risks by providing compensation that could lead to a material financial loss; 4) requiring policies and procedures for incentive-based compensation arrangements that are commensurate with the size and complexity of the institution; and 5) requiring annual reports on incentive compensation structures to the institution's appropriate Federal regulator.

Comments on the proposed rule will be accepted for 45 days after publication in the Federal Register. Although the FDIC Board acted on the proposal today, the proposal is a joint rule making by the five federal members of the Federal Financial Institutions Examination Council (FFIEC), the Securities Exchange Commission (SEC) and the Federal Housing Finance Agency (FHFA), who must each independently approve the proposed rule before it is published in the Federal Register.

Attachment:
Notice of Proposed Rulemaking on Incentive-Based Compensation Arrangements - PDF (PDF Help)