

**Supporting Statement  
Incentive-Based Compensation Arrangements  
(3064-NEW)**

Introduction

The Federal Deposit Insurance Corporation (FDIC) is requesting approval for the collection of information relating to the notice of proposed rulemaking, Incentive-Based Compensation Arrangements, which are proposed rules to implement section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). The proposed rule would require the reporting of incentive-based compensation arrangements by a covered financial institution, and prohibit incentive-based compensation arrangements at a covered financial institution that provide excessive compensation or that could expose the institution to inappropriate risks that could lead to material financial loss. The proposed rule appears at 76 Fed. Reg. 21,170 (April 14, 2011).

This is an interagency rule being proposed jointly by the FDIC along with the OCC, Board, OTS, NCUA, SEC, and the FHFA (collectively, the “Agencies”). In accordance with section 3512 of the Paperwork Reduction Act (PRA) of 1995 (44 U.S.C. § 3501-3521), agencies may not conduct or sponsor, and a respondent is not required to respond to, an information collection unless it displays a currently valid Office of Management and Budget (OMB) control number. The information collection requirements contained in the proposed rule are being submitted by the FDIC (and separately by the OCC, OTS, NCUA, and SEC) to OMB for review and approval under section 3506 of the PRA and § 1320.11 of OMB’s implementing regulations (5 C.F.R. § 1320).<sup>1</sup>

The proposed rule contains requirements subject to the PRA. The reporting requirements are found in proposed § 372.4 and the recordkeeping requirements are found in proposed §§ 372.5(b)(3)(ii)(B), 372.6(a), and 372.6(b)(5).

**A. Justification.**

**1. *Circumstances that make the collection necessary:***

The Dodd-Frank Act (Pub. L. 111-203, section 956, 124 Stat. 1376, 2011-2018 (2010)), which was signed into law on July 21, 2010, requires the FDIC and the other noted agencies to jointly prescribe regulations or guidelines with respect to incentive-based compensation practices at covered financial institutions. Specifically, section 956 of the Dodd-Frank Act (codified at 12 U.S.C. 5641) requires that the Agencies prohibit incentive-based payment arrangements, or any feature of any such arrangement, at a covered financial institution that the Agencies determine encourages inappropriate risks by a financial institution by providing excessive compensation or

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<sup>1</sup> The FHFA has concluded that the proposed rule does not contain any information collected from Fannie Mae, Freddie Mac and the Federal Home Loan Banks, including the Office of Finance, that requires the approval of OMB under the Paperwork Reduction Act (44 U.S.C. § 3501 et seq.). The Board reviewed the proposed rule under the authority delegated to the Board by OMB.

that could lead to material financial loss. Under the Dodd-Frank Act, a covered financial institution must disclose the structure of its incentive-based compensation arrangements to its appropriate Federal regulator in a manner sufficient to enable the Agencies to determine whether the structure provides “excessive compensation, fees, or benefits” or “could lead to material financial loss” to the institution. The Dodd-Frank Act does not require a covered financial institution to report the actual compensation of particular individuals as part of this requirement. The proposed rule would supplement existing rules, guidance, and ongoing supervisory efforts of the Agencies.

This proposed rule contains provisions to implement the Act, including disclosure and recordkeeping requirements that are designed to ensure that incentive compensation arrangements at a banking organization do not encourage employees to take excessive risks. The proposed rule has the following components, among others:

- Generally, the proposed rule would prohibit incentive-based compensation arrangements at a covered financial institution that encourage executive officers, employees, directors, and others to expose the institution to inappropriate risks by providing the covered person excessive compensation. The proposed rule would establish a deferral requirement for incentive awards paid to executive officers at larger covered financial institutions (i.e., generally those with \$50 billion or more in total consolidated assets), require the annual reporting to the regulator of a narrative description of the institution’s incentive compensation arrangements, and require the maintenance of adequate policies and procedures to ensure the Act’s purposes are being met.
- More specifically, section 956(a)(1) of the Dodd-Frank Act requires that a covered financial institution submit an annual report to its appropriate Federal regulator disclosing the structure of its incentive-based compensation arrangements that is sufficient to determine whether the incentive-based compensation structure provides covered persons with excessive compensation, fees, or benefits, or could lead to material financial loss to the covered financial institution. In order to fulfill this requirement, the proposed rule would establish the general rule that a covered financial institution must submit a report to its appropriate Federal regulator, on an annual basis, that provides a clear narrative description of the components of the covered financial institution's incentive-based compensation arrangements applicable to covered persons, such report must provide a succinct description of the institution’s policies and procedures governing its incentive-based compensation arrangements, and for larger institutions, a succinct description of any specific incentive compensation policies and procedures for the institution’s executive officers and other persons that the board (or a committee thereof) determines individually have the ability to expose the institution to possible losses that are substantial in relation to the institution’s size, capital, or overall risk tolerance. This information will include the specific reasons why the institution believes the structure of its incentive-based compensation plan does not encourage inappropriate risks by the covered financial institution by providing covered persons with excessive compensation or

incentive-based compensation that could lead to material financial loss to the institution, and will identify any material changes to the covered financial institution's incentive-based compensation arrangements and policies and procedures made since the institution's last report was submitted.

- The proposed rule would establish a deferral requirement for incentive awards to executives at larger covered financial institutions (i.e., generally those with \$50 billion or more in total consolidated assets). Because other individuals at a larger covered financial institution (in addition to the institution's executive officers) may have the ability to expose the institution to possible losses that are substantial in relation to the institution's size, capital, or overall risk tolerance, the proposed rule would require that, at a larger covered financial institution the board of directors, or a committee thereof, must identify those covered persons (other than executive officers) that individually have the ability to expose the institution to possible losses that are substantial in relation to the institution's size, capital, or overall risk tolerance. The proposal notes that these covered persons may include, for example, traders with large position limits relative to the institution's overall risk tolerance and other individuals that have the authority to place at risk a substantial part of the capital of the covered financial institution. The proposed rule would require that the institution's board of directors, or a committee thereof, approve the incentive-based compensation arrangement for such individuals, and maintain documentation of that approval.
- The proposed rule would require covered financial institutions to maintain policies and procedures -- appropriate to their size, complexity, and use of incentive-based compensation -- to help ensure compliance with these requirements and prohibitions. These policies and procedures must provide that the institution maintains sufficient documentation of the institution's processes for establishing, implementing, modifying, and monitoring incentive-based compensation arrangements sufficient to enable the institution's appropriate Federal regulator to determine the covered financial institution's compliance with section 956 of the Act and the rule. The Agencies would expect the documentation maintained by a covered financial institution under the proposed rule to at least include a copy of the covered financial institution's incentive-based compensation arrangement(s) or plan(s), the names and titles of individuals covered by such arrangement(s) or plan(s), a record of the incentive-based compensation awards made under the arrangement(s) or plan(s), and records reflecting the persons or units involved in the approval and ongoing monitoring of the arrangement(s) or plan(s).

## **2. *Use of the information:***

Under the Dodd-Frank Act, a covered financial institution must disclose to its appropriate Federal regulator the structure of its incentive-based compensation arrangements sufficient to allow the regulator to determine whether the structure provides excessive compensation, fees, or benefits or could lead to material financial loss to the institution. In developing the proposed

reporting provisions, the Agencies have taken into account that substantially all the covered financial institutions are already supervised and/or subject to examination by one or more of the Agencies. Accordingly, in the proposed rule, the Agencies have tailored the annual reporting requirement to the types of information that would most efficiently assist the relevant Agency in determining whether there are any areas of potential concern with respect to the structure of the covered financial institution's incentive-based compensation arrangements.

Consistent with section 956, incentive-based compensation arrangements at a covered financial institution should balance risk and financial rewards in a manner that does not provide covered persons with incentives to take inappropriate risks that could lead to material financial loss at the covered financial institution, are compatible with effective controls and risk management, and are supported by strong corporate governance. The proposed information collection is needed to enable supervisory authorities to determine whether the covered institution's incentive-based compensation arrangements and structures meet these section 956 requirements. The Agencies would deem an incentive-based compensation arrangement to be balanced when the amounts paid to a covered person appropriately take into account the risks, as well as the financial benefits, from the covered person's activities and the impact of those activities on the covered financial institution. Moreover, as to the required policies and procedures, given that the determinations to be made regarding incentive-based compensation are fact-specific, the Agencies believe that effective documentation of the covered financial institution's policies, procedures and actions related to incentive-based compensation is essential both to help promote the risk-based discipline that section 956 of the Act seeks to foster with respect to covered financial institutions, and to facilitate meaningful oversight and examination.

Generally, each Agency has reporting, examination and enforcement authority for substantially all of the covered financial institutions under its respective jurisdiction that the Agency may use if the information provided under section 956 were to indicate that the structure of a covered financial institution's incentive-based compensation arrangements may provide excessive compensation or encourage inappropriate risk-taking. In this way, the proposed rule seeks to achieve the objective of section 956 in a manner that limits unnecessary reporting burden on covered financial institutions and leverages the existing supervisory framework for institutions.

### ***3. Consideration of the use of improved information technology:***

Covered institutions may use information technology that permits the filing of reports as specified in the proposal. Covered institutions may use information technology that permits the documented review and approval of incentive compensation arrangements and awards as required of institutions' boards or committees, the deferral of awards and adjustments to awards, the designation of employees and approval of awards as required to be documented consistent with the proposal, and that permits the development, maintenance, and approval by the board (or committee thereof) of necessary policies and procedures -- all to the extent that such technology would permit review by FDIC examiners.

### ***4. Efforts to identify duplication:***

The required information as to incentive-based compensation arrangements is unique and is not duplicative of any other information already collected. As expressly stated in the proposal, with regard to the annual reporting requirement, the Agencies have tailored the annual reporting requirement to the types of information that would most efficiently assist the relevant Agency in determining whether there are any areas of potential concern with respect to the structure of the covered financial institution's incentive-based compensation arrangements. Moreover, the proposal has specified that such reporting should indicate any material changes to the covered institution's incentive-based compensation arrangements and policies and procedures made since the institution's last report was submitted (in effect, possibly eliminating some duplication in the reporting from one year to the next).

**5. *Minimizing Burden on Small Entities:***

The proposed collection will not have a significant impact on a substantial number of small entities. The proposed rules would not apply to either (1) financial institutions with less than \$1 billion in assets, or (2) institutions that do not employ incentive-based compensation arrangements. Moreover, smaller institutions commonly have less complex incentive-based compensation arrangements (and employees to whom such arrangements might apply), if any, placing less burden on smaller entities.

**6. *Consequences of Less Frequent Collections:***

Conducting the proposed information collection less frequently would be inconsistent with the provisions of the Dodd-Frank Act and significantly hinder Agency efforts to prohibit incentive-based compensation arrangements at covered financial institutions that provide excessive compensation that could expose the institution to inappropriate risks that could lead to material financial loss, or could potentially present safety and soundness risks.

**7. *Special Circumstances:***

None.

**8. *Consultation with Persons Outside the FDIC:***

On April 14, 2011, the FDIC published this proposed rule in the Federal Register for public comment. The comment period for this notice will expire on May 31, 2011.

**9. *Payment or gift to respondents:***

None.

**10. *Any assurance of confidentiality:***

To the extent that the FDIC collects the information during an examination, confidential treatment may be afforded to the records under exemptions 4 or 8 of the Freedom of Information Act, 5 U.S.C. § 552(b)(4), (8).

**11. Justification for questions of a sensitive nature:**

There are no questions of a sensitive nature.

**12. Burden estimate:**

Respondents: 301 institutions (12 institutions with total consolidated assets of \$50 billion or more and 289 institutions with total consolidated assets between \$1 billion and \$50 billion; 4,466 institutions with total consolidated assets below \$1 billion are exempt).

Burden per respondent for initial set up: 180 hours for institutions with \$50 billion or more in total assets (80 hours for reporting requirements and 100 hours for recordkeeping requirements) and 70 hours for institutions between \$1 billion and \$50 billion in total assets (30 hours for reporting requirements and 40 hours for recordkeeping requirements).

Burden per respondent for ongoing compliance: 70 hours for institutions with \$50 billion or more in total assets (40 hours for reporting requirements and 30 hours for recordkeeping requirements) and 25 hours for institutions between \$1 billion and \$50 billion in total assets (15 hours for reporting requirements and 10 hours for recordkeeping requirements).

**Total FDIC annual burden: 30,455 hours** (22,390 hours (12X180+289X70) for initial set-up and 8,065 hours (12X70+289X25) for ongoing compliance).

**13. Estimate of total annual costs to respondents:**

Not applicable.

**14. Estimate of annualized costs to the Federal government:**

Not applicable.

**15. Change in burden:**

This is a new collection.

**16. Information regarding collections whose results are to be published for statistical use:**

The FDIC has no plans to publish the information for statistical purposes.

**17. Display of Expiration Date:**

Not applicable.