Supporting Statement
Guidance on Sound Incentive Compensation Practices
OMB Control No. 1557-0245

A. Justification.

1. Circumstances that make the collection necessary:

Incentive compensation practices in the financial services industry contributed to the financial crisis that began in 2007. Bank employees too often were rewarded for increasing short-term revenue or profit without adequate regard to the risks taken to achieve those results. These practices exacerbated the risks and losses at a number of banking organizations and resulted in the misalignment of the interests of employees with the long-term safety and soundness of their organizations. The Guidance on Sound Incentive Compensation Practices (Guidance) fulfilled the commitment made by President Obama and the Department of the Treasury at the G-20 meeting in September 2009 to implement the Financial Stability Board's Compensation Principles.[1]

The Guidance is based on three key principles that are designed to ensure that incentive compensation arrangements at a banking organization do not encourage employees to take excessive risks. These principles provide that incentive compensation arrangements should:

- Provide employees incentives that do not encourage excessive risk-taking beyond the organization's ability to effectively identify and manage risk;
- Be compatible with effective controls and risk management; and
- Be supported by strong corporate governance, including active and effective oversight by the organization's board of directors.

The Guidance and its underlying principles are consistent with the Principles for Sound Compensation Practices adopted by the Financial Stability Board (FSB) in April 2009, as well as the Implementation Standards for those principles issued by the FSB in September 2009.

The Guidance promotes the prompt improvement of incentive compensation practices in the banking industry by providing a common prudential foundation for incentive compensation arrangements across banking organizations and promoting the overall movement of the industry towards better practices. Supervisory action plays a critical role in addressing misaligned compensation incentives, especially where issues of competition may make it difficult for individual firms to act alone. With the application of the Guidance, supervisors help to better align the interests of managers and other employees with the long-term health of the organizations for which they work while also relieving any competitive concerns among the banking organizations.

[1] 75 FR 36395 (June 25, 2010).

2. Use of the information:

The Guidance helps to ensure that incentive compensation policies at national banks and Federal savings associations do not encourage excessive risk-taking and are consistent with the safety and soundness of the organization. Under the Guidance, each national banks and Federal savings association is required to:

- For a large national bank or Federal savings association, have policies and procedures that identify and describe the role(s) of the personnel and units authorized to be involved in developing and administering incentive compensation arrangements, identify the source of significant factors of compensation that are sensitive to risk, establish appropriate controls governing these factors, and identify the individual(s) and unit(s) whose approval is necessary for the establishment or modification of incentive compensation arrangements;
- Create and maintain sufficient documentation to permit an audit of the organization's processes for developing and administering incentive compensation arrangements;
- Have any material exceptions or adjustments to the incentive compensation arrangements established for senior executives approved and documented by its board of directors; and
- For a large national bank or Federal savings association, have its board of directors receive and review, on an annual or more frequent basis, an assessment by management of the effectiveness of the design and operation of the organization's incentive compensation system in providing risk-taking incentives that are consistent with the organization's safety and soundness.

3. Consideration of the use of improved information technology:

National banks and Federal savings associations may use any information technology that permits review by OCC examiners.

4. Efforts to identify duplication:

The required information is unique and is not duplicative of any other information already collected.

5. If the collection of information impacts small businesses or other small entities, describe any methods used to minimize burden.

There are no alternatives that would result in lowering the burden on small institutions, while still accomplishing the purpose of the guidance.

6. Consequences to the Federal program if the collection were conducted less frequently:

Conducting the collection less frequently would present safety and soundness risks.

7. Special circumstances that would cause an information collection to be conducted in a manner inconsistent with 5 CFR Part 1320:

The information collection will be conducted in a manner consistent with 5 CFR Part 1320.

8. Efforts to consult with persons outside the agency:

On July 27, 2016, the OCC issued a 60-day notice soliciting comment on the information collection, 81 FR 49356. One comment was received from an individual.

The commenter stated that the burden estimates are low, unrealistic and unsupported by empirical evidence. The commenter requested that the next notice explain how the burden estimates were calculated and the empirical evidence used in the calculation.

The commenter believes that the requirements in the guidance requiring institutions to have policies, procedures, appropriate controls, and sufficient documentation to permit an audit of the incentive compensation arrangements and for the board of directors to review, at least annually, an assessment of the effectiveness of the design and operation of the bank's incentive compensation system to ensure safety and soundness would likely be met by having the internal audit department examine incentive compensation systems and provide reports to the board audit committee. The commenter estimates that, in institutions with $20 billion or more in total assets, a minimum of four internal auditors customarily spend three or four weeks auditing the effectiveness of the design and operation of incentive compensation systems resulting in an annual assessment of the effectiveness of the design and operation of the bank's incentive compensation system at large banks taking a minimum of 640 hours to complete. The commenter also stated that this estimate would not include additional hours needed every year to: (i) update policies; (ii) revise procedures; (iii) adjust controls; and (iv) document annual incentive payments and document approvals. The commenter believes that, in large, systemically important institutions, internal auditors can spend one to two thousand hours auditing the many incentive compensation plans for compliance with OCC requirements.

The commenter also believes that the estimate for "small banks" is also grossly underestimated and that, in a small bank ($50 million in total assets), it would take one person at least one week to assess the effectiveness of the design and operation of the compensation systems and format the results to be submitted to the board of directors. This would be in addition to the 40 hours needed to update written policies and procedures, document annual incentive payments, and document approvals.

The OCC uses the legal standard for estimating burden hours under the PRA (44 U.S.C. 3502(2)). The term "burden" means time, effort, or financial resources expended by persons to generate, maintain, or provide information to or for a Federal agency, including the resources expended for: (a) Reviewing instructions; (b) acquiring, installing, and utilizing technology and systems; (c) adjusting the existing ways to comply with any previously applicable instructions and requirements; (d) searching data sources; (e) completing and reviewing the collection of information; and (f) transmitting, or otherwise disclosing the information. The OCC believes that its burden estimates are accurate, given that institutions already have the required arrangements in place, including any required systems and procedures.

The banking agencies[2] estimated in their original notice[3] that large institutions would spend 480 hours to modify their policies and procedures to monitor incentive compensation. Small institutions would spend 80 hours to establish or modify policies and procedures to monitor incentive compensation. Forty hours would be required to maintain an incentive compensation program.

In the experience of the banking agencies, two months is typically required for a large institution to set up a program of this complexity and one business week is required for yearly maintenance. The banking agencies generated these estimates based on their experience with other information collections.

9. Payment or gift to respondents:

None.

10. Any assurance of confidentiality:

The information is kept confidential to the extent permitted by law.

11. Justification for questions of a sensitive nature:

There are no questions of a sensitive nature.

12. Burden estimate:

Estimated Number of Respondents: 41 large banks; 1,381 small banks.

Estimated Burden per Respondent: 520 hours (480 for setup; 40 for yearly maintenance) for large banks; 120 hours (80 for setup; 40 for yearly maintenance) for small banks.

Frequency of Response: Annually.

Total Annual Burden: 187,040 hours.

13. Estimate of total annual costs to respondents (excluding cost of hour burden in Item #12):

Not applicable.

14. Estimate of annualized costs to the Federal government:

Not applicable.

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[2] OCC, Board of Governors of the Federal Reserve System, and Federal Deposit Insurance Corporation.
[3] 75 FR 36395 (June 25, 2010).

15. Change in burden:

Former Burden:

3,024 respondents; 640,692 hours.

New Burden:

1,422 respondents; 187,040 hours.

Difference:

-1,602 respondents; - 453,652 hours.

The reduction in burden is due to the decrease in the number of regulated entities.

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

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

17. Reasons for not displaying OMB approval expiration date:

The OCC will display the OMB approval expiration date.

18. Exceptions to the certification statement:

Not applicable.

B. Collections of Information Employing Statistical Methods.

This information collection does not employ statistical methods.