Center for Capital Markets Competitiveness

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February 17, 2010

Mr. Robert E. Feldman
Executive Secretary,
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Re: Advance Notice of Proposed Rulemaking
RIN 3064-AD56

Dear Mr. Feldman:

The U.S. Chamber of Commerce is the world's largest business federation, representing more than three million businesses and organizations of every size, sector, and region. The Chamber has created the Center for Capital Markets Competitiveness (the "CCMC") to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy. To achieve this objective, it is an important priority of the CCMC to advance an effective and transparent corporate governance structure.

The CCMC welcomes this opportunity to comment on the Advance Notice of Proposed Rulemaking (the "Proposed Rulemaking") issued by the Federal Deposit Insurance Corporation (the "FDIC") on January 12, 2010 on ways that the FDIC's risk-based deposit insurance assessment system could be changed to account for the risks posed by certain employee compensation programs. We note that, as set forth in the proposed rulemaking, the FDIC is exploring whether and, if so, how to incorporate employee compensation criteria into the risk-based assessment system. We further note that the FDIC is not seeking to limit the amounts which employees are compensated, but instead to adjust risk-based deposit insurance assessment rates to adequately compensate the Deposit Insurance Fund for the risks inherent in the design of certain compensation programs.

While the CCMC notes that the FDIC has decided to examine the role of employee compensation in evaluating the strength of depository institutions, we believe that, in the current environment, any policy-making should be carefully considered. Indeed, as we explain below, the FDIC has failed to thoroughly study the issues of compensation and inappropriate risk taking. Indeed, the FDIC did not list compensation as an issue that needed to be addressed as the result of the financial crisis. Therefore, the proposed rule making suggests a solution without exploring if there is a problem, or how such a problem, if it exists, should be resolved.

As a result and in view of the other legislative and regulatory initiatives underway, the CCMC recommends that the FDIC direct its immediate efforts towards addressing other – and potentially more critical issues related to the financial crisis and restoring financial stability.

Proposed Rulemaking Should Be Guided by Consensus Principles

It is well-recognized that effective corporate governance is a cornerstone of every successful company. At its core, this involves the establishment and maintenance of policies and practices that promote an ongoing dialogue between executives, directors, and shareholders that ensures continued focus on the company's business objectives and, ultimately, long-term value creation. The policies and practices used to determine employee compensation are an integral part of this process.

Last year, the Chamber presented Treasury Secretary Timothy F. Geithner with a set of principles, crafted in consultation with businesses and investors, that we believe are consistent with these objectives and, therefore, should guide the development of any corporate governance and compensation-related reforms. These principles are as follows:

- Corporate governance policies must promote long-term shareholder value and profitability, but should not constrain reasonable risk-taking and innovation.

- Long-term strategic planning should be the foundation of managerial decision-making.

- Corporate executives' compensation should be premised on a balance of individual accomplishment, corporate performance, adherence to risk management, and compliance with laws and regulations, with a focus on shareholder value.

- Management needs to be robust and transparent in communicating with shareholders.

In presenting these principles, the Chamber stated that: "[t]hese principles provide a template for policies that would allow for reasonable risk-taking, continued innovation, the ability to acquire and retain talent, and protect investor rights".

The CCMC recommends that any policy initiatives undertaken by the FDIC to alter its risk-based assessment system be guided by the foregoing principles, or similar principles that reflect the consensus views of the principal stakeholders in the corporate governance process.

FDIC Policy-Making and the Proposed Rulemaking

The safety and soundness of our financial institutions are of fundamental importance to our economy. Capital formation is a key factor in job creation and a failure to have functioning and efficient markets will adversely impact long-term economic growth and overall prosperity. Thus, it is vitally important that our policy-makers, such as the FDIC, take the necessary steps to ensure the stability of our financial sector. At the same time, the potential unintended consequences that may result from any potential regulatory initiatives also need to be carefully considered and weighed.

On January 11, 2010, by a 3-2 vote, the FDIC approved the publication of the Proposed Rulemaking. In announcing the Proposed Rulemaking, FDIC Chairman Bair stated, "The recent crisis has shown that compensation practices that encourage excessive risk can create significant losses in the financial system and the deposit insurance fund."[1]

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[1] FDIC Press Release of January 11, 2010, **FDIC Board Seeks Comment on Incorporating Employee Compensation Structures Into the Risk Assessment System**.

It is beyond dispute that the U.S. banking system has undergone severe stresses following the financial crisis and the ensuing recession. Yet it remains unclear precisely whether and, if so, to what extent the compensation policies and practices within the financial sector contributed to these stresses. Although over 160 FDIC-supervised banks have failed since the collapse of Lehman Brothers, it does not appear that the FDIC (or, for that matter, any other banking or financial regulator) has conducted a comprehensive analysis of the executive compensation policies and practices of those institutions to assess the impact of those policies and practices on their demise and ultimate failure.

Further, while the FDIC has noted that of the 49 Material Loss Reviews completed in 2009 that addressed the factors contributing to the losses resulting from the financial institutions failures, 17 cited employee compensation practices as a contributing factor, based on the Proposed Rulemaking's objective of identifying compensation-related criteria upon which to base adjustments to the risk-based assessment system, it does not appear that the FDIC has yet determined how those practices contributed to the institutions' problems and whether their presence or absence will have a material impact on their overall strength and viability.

We are concerned that the Proposed Rulemaking assumes a need to promote specific compensation policies and practices (and, concomitantly, to discourage specific policies and practices) without first conducting a thorough analysis to determine whether, in fact, compensation structures were a material contributing factor in recent financial institution failures.

We note that, in identifying the issues emerging from the financial crisis, the FDIC did not list executive compensation as one of them.[2] In fact, in publicly announcing the lessons of the financial crisis, the FDIC identified only the following issues - underwriting, consumer protection, capital, concentrating risk, liquidity, and public stakeholders – as areas that needed to be addressed.[3] While it may be appropriate to now add compensation to this list, the CCMC believes that the original

[2] See, ***Supervisory Insights***, summer 2009, Volume 6, Issue 1, **A Year of Banking Supervision 2008 and a Few of its Lessons**; See also the corporate governance section of the FDIC website which does not discuss executive compensation in outlining director responsibilities, specifically, ***5000-Statement of Policy***, **Statement Concerning the Responsibilities of Bank Directors and Officers.**

[3] ***Supervisory Insights***, summer 2009, Volume 6, Issue 1, **A Year of Banking Supervision 2008 and a Few of its Lessons.**

issues reflect areas of greater concern and should have a higher priority than any compensation-related issues.

Further, the CCMC is concerned that the Proposed Rulemaking, particularly when combined with the absence of empirical information about the compensation policies and practices of financial institutions, specifically those of the failed FDIC-supervised institutions, may lead to misguided policies based on unsubstantiated assumptions that ultimately will prove harmful to the banking system and the capital markets overall. For example, the FDIC requests input on whether an adjustment to risk-based assessment rates should be made if certain compensation practices are followed with respect to the payment of bonuses, such as the awarding of guaranteed bonuses, granting bonuses that are disproportionate in amount to base salary, or paying bonuses in a single lump-sum.

While each of the cited practices can be woven into a situation that would demonstrate excessive risk, they can be – and typically are – legitimate reasons for a company to employ any of these practices. Consequently, a policy that applies a positive or negative value to the presence or absence of such practices, which would then be used to adjust an institution's risk-based assessment rate would be either arbitrary and capricious or require such a level of familiarity and understanding of the institution's compensation history, philosophy, and specific situation as to be practically unworkable. This could easily lead to a change in compensation practices that would be compliance-driven, rather than market-driven, with attendant unforeseeable consequences.

We also note that the recent decision of the Securities and Exchange Commission to require all public companies to assess the risk profile of their employee compensation programs and provide disclosure about any material adverse risks that may affect the company underscores the influence of the banking and financial regulators when it comes to compensation-related risk matters. Many companies view regulators such as the FDIC, which have greater experience in overseeing risk-based evaluations, as offering useful guidance in helping them to frame their own risk assessments. Consequently, potentially significant rulemaking, which may have an impact well beyond just the financial sector, without a thorough understanding of current problems and challenges, the complex implications of various alternative solutions, the overlapping regulatory coverage of executive compensation, and the rapidly evolving corporate governance landscape is, at best,

problematic and, at worst, dangerous. The split vote authorizing the Proposed Rulemaking reflects the challenges that are presented in addressing this area and should signal the need for caution and more deliberative action before proceeding.

Consequently, before taking action to influence that compensation policies and practices of depository institutions, the CCMC urges the FDIC to first consider the potential implications of endorsing any specific compensation policies and practices, as well as the need for and cumulative impact of these policies and practices when added to the initiatives already being considered by other banking and financial regulators, so that any harmful broad macro-economic consequences can be identified and mitigated. Accordingly, we request that the Proposed Rulemaking be withdrawn until such time as the FDIC has properly studied and considered these matters.

<u>Retention and Acquisition of Talent</u>

Human capital is the operating infrastructure of a financial institution. The quality of the workforce and ability to attract and retain talent are long-term indicators of a financial institution's ability to be successful and achieve and maintain profitability. The FDIC recognizes that talent acquisition and retention is essential for properly functioning banks, particularly those banks that are undergoing severe stress.

In outlining the responsibilities of bank directors and officers, the FDIC has stated that:

> Banks need to be able to attract and to retain experienced and conscientious directors and officers. When an institution becomes troubled, it is especially important that it have the benefit of the advice and direction of people whose experience and talents enable them to exercise sound and prudent judgment.... This means that directors are responsible for selecting, monitoring, and evaluating competent management; establishing business strategies and policies;[4]

Clearly, the FDIC recognizes that the attraction, retention, and motivation of talent are central to a bank's ability to properly function and compete in today's global markets. Appropriate compensation practices that allow employees to engage in

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[4] ***5000-Statement of Policy*, Statement Concerning the Responsibilities of Bank Directors and Officers,** www.FDIC.gov.

reasonable risk-taking and long-term decision-making are of great importance. Narrowing or restricting the compensation policies and practices of a financial institution has the potential to drive away talent, degrade its foundation, and undermine the long-term viability of the business. The compensation standards imposed on participants in the Treasury Department's Troubled Asset Relief Program ("TARP") provide a clear example of this risk.

In commenting on the TARP Standards for Compensation and Corporate governance, the CCMC noted that:

> The evaluation of compensation and governance policies for TARP companies should be done with an eye to providing those companies with the tools and talent needed to be successful over the long-term. TARP recipients must be able to compete in the marketplace. To do so, they must be able to attract and retain needed talent. If their compensation programs are not competitive, their ability to leave TARP will be impaired. The unfortunate reality is that TARP companies are already at a disadvantage. There have been press reports throughout the year have indicated that foreign firms such as Deutsche Bank, UBS and others have been drawing talented individuals away from TARP firms....Therefore, the principles should be amended to contain a principle on the competitiveness of TARP companies.

Recent press reports (see attachments) have documented the flight of talent from TARP participants that has occurred before and since the Treasury Department's Special Master, Kenneth Feinberg, began issuing his compensation decisions for the firms receiving exceptional assistance. The *Washington Post* has reported that in two firms, close to a majority of the top 25 most highly paid executives departed before the Special Master's rulings were even announced. Further, it has been reported by *Bloomberg News* and other media outlets that Mr. Feinberg has stated that he is "very concerned" that his rulings will drive talent away from firms.

Actions have consequences and the competition for talent is fierce. As we have seen on numerous occasions, employees can easily be lured away by direct competitors, global firms, or different industries. Accordingly, the flight of talent from financial institutions to unregulated entities, such as private equity firms, mutual

funds, hedge funds, or foreign companies is a genuine risk, particularly for the financial institutions whose compensation practices will be directly affected by the Proposed Rulemaking.

The CCMC is concerned that the Proposed Rulemaking fails to analyze the potential impact that it will have on the competition of talent within the financial sector or the impact on the potential loss of talent at affected financial institutions. We believe that a loss of talent can be as devastating to a firm as the effects of excessive risk taking. Accordingly, we request that the Proposed Rulemaking be withdrawn until such time as the FDIC has properly studied and considered the impact of incorporate employee compensation criteria into the risk-based assessment system on talent acquisition and retention.

The Roles of the Director and Shareholder

The CCMC respects the critical role that the FDIC plays in ensuring the safety and soundness of insured financial institutions. It must not be forgotten, however, that directors and shareholders also share a unique and vital responsibility in the proper oversight of a financial institution.

The CCMC is concerned that the introduction of a standard set of employee compensation criteria into the risk-based assessment system, in addition to threatening the stability of a financial institution's human capital as discussed above, will undermine the ability of directors and shareholders to collectively develop solutions to risk-based issues that are best suited for their particular situations. We firmly believe that directors and shareholders should, within their prescribed regulatory framework, retain the ability to choose the corporate governance and employee compensation structures that work best for their firm. This ability to experiment with various approaches leads to a diversity of structures and practices that can then be tailored to best suit each specific financial institution. While this may provide firms with a competitive edge, it also creates a more dynamic and productive capital markets system.

As evidenced by past examples, a "one size fits all" approach inevitably discourages innovation, reduces diversity, and inhibits the efficiency of our capital markets. Accordingly, the CCMC recommends that, in further studying employee compensation issues, the FDIC should work closely with organizations representing

directors and shareholders to better understand and further the dynamics of this relationship. We further recommend that, in considering future rulemaking, the FDIC be careful to not inhibit the director-shareholder dialogue and, instead, tailor any rulemaking to reinforce this relationship.

Federal Reserve and Legislative Efforts

The Federal Reserve has developed and solicited public comment on its own proposed supervisory guidance on compensation issues.[5] To minimize any adverse impact on or duplicative or redundant efforts affecting the financial markets, the CCMC recommends that the FDIC defer action on the Proposed Rulemaking unless and until it has had an opportunity to coordinate its actions with the Federal Reserve. We are concerned that, if the Federal Reserve and the FDIC were to develop overlapping or conflicting policies on monitoring and managing compensation-related risk, confusion would ensue and the potential for "regulatory arbitrage" will increase. Such an outcome would not only undermine the integrity of the financial system, it would give financial institutions an incentive to probe the gaps and weaknesses of the dual regulatory frameworks, thereby jeopardizing the prospects for a smooth transition to any new requirements.

While the FDIC views the Proposed Rulemaking to be complementary to the Federal Reserve's initiatives, we question whether the contemplated standards would truly be viewed as "voluntary" by depository institutions. To the extent that the contemplated standards resulted in higher risk-based assessment rates for institutions that did not meet any new standards, it would place them at a competitive disadvantage in an area where, at present, there is no clear consensus that certain policies and practices result in greater levels of risk. Thus, we believe that such "voluntary" standards would quickly become the accepted norm for all financial institutions, whether or not they produce a tangible benefit to the firm or its stakeholders. Further, given the Federal Reserve's pronouncements to date, we question whether the contemplated standards would differ in any material way from the supervisory initiatives that it is likely to adopt. Ultimately, we are concerned that the FDIC has not presented a persuasive argument that its actions are necessary given the pending initiatives of the Federal Reserve.

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[5] Board of Governors of the Federal Reserve System, **Proposed Guidance on Sound Incentive Compensation Policies, Docket Number OP-1374**

Further, we note that the principal financial regulatory reform proposals working their way through Congress contain numerous corporate governance and compensation-related provisions, which, if enacted, have the potential to dramatically change the regulatory and operating environment for financial institutions and other companies. The CCMC believes that it would be imprudent to introduce a new and potentially complex set of risk-related requirements at a time when significant legislative action is imminent. Until the corporate governance landscape has stabilized, we believe that the time is not ripe to introduce another set of standards that would impact executive and employee compensation.

Finally, we note that Congress has under consideration legislative proposals that may impact compensation. For example, H.R. 4173, the Wall Street Reform and Consumer Protection Act of 2009, which was approved by the House of Representatives in December 2009, contain a provision that would require greater independence on the part of a board compensation committee and the use of independent compensation professionals. Similarly, numerous bills have been introduced in Congress that would require companies to adopt a compensation recovery ("clawback") policy, a practice that is widespread among large public companies. Finally, we note that numerous companies already provide for the payment of significant portions of their long-term incentive compensation in the form of shares of their common stock; often subject to additional vesting restrictions. Yet, it should be noted that none of these legislative proposals have become law, other than those requirements for firms that received assistance through the TARP program.

Prescriptive rulemaking by a regulatory agency before there is, or is not, legislative action is premature. It behooves the FDIC to allow the legislative process to play out before regulatory action is undertaken. Accordingly, we request that the Proposed Rulemaking be withdrawn until such time as these other initiatives have had an opportunity to become operative and their impact assessed and understood.

Small and Regional Banks

The CCMC believes that, before undertaking any rulemaking, the FDIC should study the potential impact that any compensation-related changes to its risk-based assessment system would have on smaller and regional banks. As is often the case, it appears that the Proposed Rulemaking would be more burdensome for smaller and

regional banks. These banks face different issues and problems than larger financial institutions and we believe that it would be prudent to consider and address their special needs as part of any proposed rulemaking. The purpose of this study should be to adapt any contemplated rulemaking to the requirements of smaller and regional banks, consistent with the goals of the FDIC.

Conclusion

Once again, the CCMC would like to thank the FDIC for the opportunity to comment on the Proposed Rulemaking.

In conclusion, the CCMC believes that the proposed rulemaking may be arbitrary in view of the lack of study, failure to cite the specific issues that need to be addressed, as well as the lack of appropriate timing because of potential action by Congress. Additionally, executive compensation policies under the TARP program may be harming the operation of financial institutions through a failure to retain and acquire talent. Through this rulemaking the FDIC could be going down the same path. Additionally, the role of directors and shareholders should be preserved and strengthened, while the needs of small and regional banks should be understood and addressed. Without question, financial institutions should avoid excesses that imperil the long-term viability of the firm. However, the FDIC's policies must be crafted to allow financial institutions to flourish. Profitable stable financial institutions will insure vibrant capital markets which are the engines and providers of long-term job growth. Improper rules or enforcement can create underperformance values that will harm financial institutions and hamper economic growth.

Because of the lack of study by the FDIC, the continued debate within Congress on financial regulatory reform it appears that the Proposed Rulemaking is neither well thought-out nor timely. Accordingly, the CCMC respectfully requests that this proposed rulemaking be withdrawn.

Sincerely,

Tom Quaadman
Executive Director, Financial Reporting and
Investor Opportunity
Center for Capital Markets Competitiveness
U.S. Chamber of Commerce

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Brain drain takes toll at Citi and BofA

Many top traders and bankers have left the financial giants for rivals. The trend may continue as long as Citi and BofA remain under the government's thumb.

By David Ellis, CNNMoney.com staff writer
Last Updated: June 23, 2009: 11:50 AM ET

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NEW YORK (CNNMoney.com) -- The so-called brain drain that big banks have worried about ever since the government stepped in to bail out the financial sector appears to be well underway.

And nowhere is that pain being felt more acutely than at Citigroup (C, Fortune 500) and Bank of America (BAC, Fortune 500), the two banks that have received the most aid from the government and are subject to the most onerous restrictions on executive compensation.

Last Friday, Ajay Banga, the CEO of Citigroup's Asia Pacific operations, announced his resignation from the company. Banga, a 13-year firm veteran who quickly rose through the ranks, will take up his new role as chief operating officer at the credit card processor MasterCard (MA, Fortune 500) starting in August.

Banga is perhaps the highest-profile defection from Citi as of late. But several other top bankers, traders and analysts have recently jumped ship for similar jobs at private equity giant Blackstone Group, Germany's Deutsche Bank and the boutique research shop Ladenburg Thalmann.

A day earlier, Bank of America lost one of its top investment bankers and long-time Merrill Lynch veteran William Rifkin to JPMorgan Chase (JPM, Fortune 500), representing the latest high-profile departure from the Charlotte, N.C.-based lender since it completed its purchase of the brokerage giant late last year. Other executives have left for positions at Oppenheimer & Co., Piper Jaffray and British bank Barclays.

Exact figures about the number of departures from Citi and BofA are tough to come by. Calls to both Citigroup and Bank of America requesting comment on the string of recent departures were not immediately returned.

But Citi chairman Dick Parsons conceded at an economic forum last week hosted by CNNMoney.com parent Time Warner that management has had to use terms like "patriotic duty" and the potential of doing "fascinating" work to convince people to work for the embattled firm. (Parsons was formerly the chairman and CEO of Time Warner.)

Jumping off ships still anchored by TARP

Parsons' remarks illustrate how difficult it has become for large, troubled financial institutions to attract and retain top employees -- especially those like Citi and BofA which are still part of the Treasury Department's Troubled Asset Relief Program.

"It is normal but it is exacerbated by the fact that those who are stuck in TARP can't compensate their people as well those who aren't," said Anton Schutz, president of Mendon Capital Advisors, a

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Firms that are not bound by the government restrictions have lured away talent from Citigroup and Bank of America in recent months.

Bailout tracker

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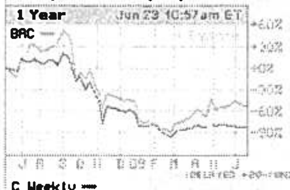
Evaporated equity



Employees of Citi and BofA have seen the value of their restricted stock and options plummet over the past year.

1. New home sales: 'Really good news'
2. Get ready for banking's next headache
3. Stocks struggle after rally
4. Don't expect earnings surprises to last
5. Bernanke: 'Economy will be stronger'

Markets	Last	Change
Dow Jones	9,049.41	-43.83 / -0.48%
Nasdaq	1,953.74	-12.22 / -0.62%
S&P 500	974.92	-4.34 / -0.44%
10-year Bond	95 2/32	Yield: 3.73%
U.S.Dollar	1 euro = $1.422	-0.001

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Despite investor concern about risk, CEO Fred Tomczyk says the

firm that invests in financial stocks.

For months, financial firms have railed against proposed compensation caps, warning it would prompt an exodus of workers at firms that remain under the government's thumb to smaller rivals, foreign banks and the lightly-regulated worlds of private equity and hedge funds.

But now that ten large financial firms, including JPMorgan Chase and Goldman Sachs (GS, Fortune 500), have been permitted to pay back TARP funds, it could become even tougher for Citi and BofA to hold on to top employees.

0.00 / 4:12 Feds changed bailout 'rules'

Last week, the White House proposed to limit bonuses for senior executives and other highly-paid employees at firms that got taxpayer assistance to one third of their total compensation.

And at Citigroup and Bank of America, both of which required "exceptional" government assistance, compensation of the top 100 salaried employees are now set to scrutinized by the newly appointed "pay czar."

Sinking stock prices haven't helped

Retaining talent, even in boom times, has never been easy for top Wall Street firms. Over the years, would-be 'masters-of-the-universe' types have been quick to jump ship if the pay, opportunities or culture of another firm was attractive enough.

"There is pretty much zero loyalty in this industry" said Peter Cappelli, a professor at the Wharton School at the University of Pennsylvania and director of its Center for Human Resources. "This would be happening whether or not there were TARP."

Still, fears about the heavy hand of government in a bank's day-to-day operations have been tough to shake for many workers.

According to a poll of more than 2,000 finance pros taken earlier this year by the online job site eFinancialCareers.com, just over half of those polled said they were likely to look for work at another financial services firm given the compensation restrictions placed on companies that received aid from the government.

The plunge in bank stock prices also could be giving some Wall Street veterans reason to seek out new jobs.

Many finance pros have watched the value of restricted stock and options whittle away in recent months. John Rogan, a partner and head of the global banking and markets practice at executive search firm Russell Reynolds Associates, said there is a common view that the value of their equity stake may never recover given how far some firms' stocks have fallen.

Shares of Citigroup and Bank of America are worth just a fraction of what they were this fall. And in the case of Citi, many shareholders are bracing for further dilution once the government officially completes the conversion of its preferred shares stake into common stock later this year as part of a broader program to beef up the bank's ailing capital levels.

Sensing that frustration, major European banks such as Deutsche Bank and Barclays (BCS), as well as boutique investment banks like Moelis & Co. and Greenhill and have successfully poached talent from Citi and BofA as well as other big U.S. banks.

But some rivals appear to be particularly targeting Citi and BofA. Five of the last 16 big hires made by Moelis in the past six months, for example, came from either Citigroup or Bank of America.

"The opportunity to move to someplace smaller where you have more control over your own destiny and therefore your own pay is extremely appealing to people these days," said Rogan.

Fighting back

Experts contend, however, that Citi, BofA and other peers that have suffered the loss of top talent, are not standing idly by while bankers and traders leave.

Even before winning their freedom from TARP, many big banks such as Morgan Stanley raised base salaries to try earlier this year to compensate for potential bonus restrictions. The *Financial Times* reported earlier this month that Citi and Bank of America are following suit with their bankers.

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In addition, experts think both lenders may be employing an approach that has become a common practice lately on Wall Street - dangling retention bonuses in front of top performers, or at the very least pledging that a bonus of some sort will be there at year's end now that some businesses, such as bond trading, are booming.

Still, there's also the issue of replacing those who have already left. Of course, Citi and BofA may look within their own ranks to fill the shoes of a top performer like Banga or Rifkin, said Jess Varughese, managing partner at the New York City-based consultancy Milestone, which focuses on the financial services industry.

In most instances, however, the new executives never quite live up to the star power of their predecessors.

"The big name leaves are very, very tough to replace," said Varughese. And that is going to make it even more critical for Citi and BofA to do what they can to hold on to their best and brightest employees. ■

First Published: June 23, 2009: 11:38 AM ET

Bad blood: The trouble with TARP

On Main Street, little hope and hiring

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Pay Day

President Obama's new, somewhat improved, executive compensation policy

Saturday, June 13, 2009

CAN IT have been only three months ago that all of Washington was apoplectic over $165 million in bonuses for executives at AIG, the federally rescued insurance firm? President Obama declared his "anger" over the AIG bonuses, and, in a fit of affected populism, the House of Representatives voted to tax away 90 percent of the AIG bonuses, along with those paid to employees of other firms that took at least $5 billion from the Treasury Department's bank bailout fund. The stage seemed set for massive and counterproductive federal intervention into corporate compensation decisions.

So the first thing that should be said about the Obama administration's new executive compensation policy, unveiled by Treasury Secretary Timothy F. Geithner on Wednesday, is that cooler heads seem to have prevailed. It relies more on improving corporate governance than on arbitrary controls and confiscatory taxes. The administration backed down from its previous proposal of a $500,000 annual salary cap at the most heavily bailed-out banks, substituting instead a limit on bonuses that affects relatively few top executives.

Probably the least helpful administration idea is to give shareholders a non-binding vote on proposed executive compensation packages. Presented as a modest step toward corporate democracy, "say on pay" may prove either empty or pernicious. If the shareholders' vote is truly non-binding, it won't change compensation practices. More likely, boards of directors, fearing bad publicity, will shape compensation policy to the anticipated opinions of shareholders, who may be greedy for short-term profits themselves -- or insufficiently informed about the finer points of retaining talent.

Britain has had "say on pay" since 2002, and the only impact was to curb severance for

underperforming executives. And why should shareholders have a say on pay as opposed to every other issue that affects their investments? If you like the way California governs by referendum, you'll love "say on pay."

The administration's plans impose the tightest controls on the companies in which the U.S. government has the biggest stake: AIG, Citigroup, Bank of America, Chrysler, GM and the carmakers' finance companies. A special master, Kenneth Feinberg, will set compensation for these firms' top 100 executives. The government has both a right and an obligation to protect its investment capital. Mr. Feinberg is an honest and experienced man armed by Treasury with "principles" that reward executive prudence.

Still, at a time when the goal is restoring these firms to profitability and ending government ownership, this is a lot of business authority to invest in one official with no expertise in, say, automobile manufacturing. If you were a promising young car executive, would you rather work for the Treasury Department or the politically unencumbered Honda? And didn't President Obama just say something about not wanting to run GM?

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The Washington Post

Cool anger over Wall Street bonuses by governing how they're handed out

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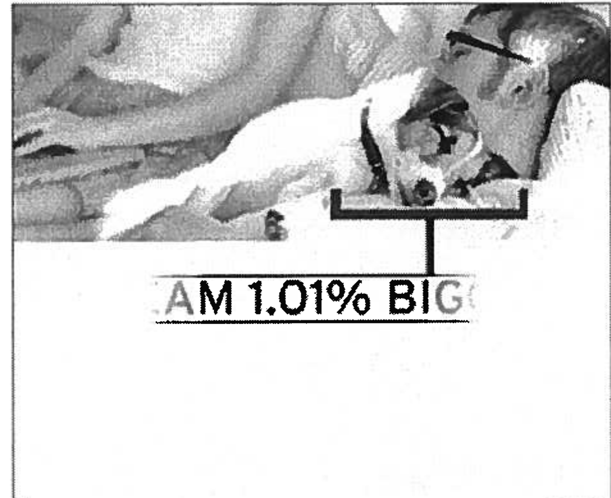

Tuesday, January 19, 2010; A16

ANOTHER Wall Street bonus season is upon us, accompanied by another round of studied outrage in Washington. White House economic adviser Christina Romer said the prospect of tens of billions of dollars in payouts "offends" her. So profound was the disgust of Andy Stern, president of the Service Employees International Union, that he could express it only in a complex metaphor: "They backed the truck up to Fort Knox in broad daylight," Mr. Stern said. "They emptied it out, we rescued them and they get $150 billion in bonuses."

How much is the right amount to pay a Wall Street trader? Perhaps no one "deserves" $5 million a year to swap bonds, especially when the financial industry has performed badly. But no one "deserves" $5 million to bat .220 for a last-place baseball team, either. There is simply no objective, scientific answer to such a question. Therefore, it is best left to market forces and the decisions of private-sector figures, such as executives and the boards of directors who are supposed to hold them accountable, on behalf of shareholders. Over time, firms have found that bonuses -- performance-linked portions of company revenue added to a base salary -- are the best way to reward and retain talent.

There are two provisos: First, government's say on pay properly grows when financial institutions are living off taxpayer support, as they have been for much of the past two years. Second, even when taxpayer support ends, the public has a legitimate interest in financial stability, including an interest in ensuring that Wall Street's pay systems -- as opposed to the amount of any particular person's pay -- are not destabilizing.

At the moment, the financial system is transitioning from massive and open government support for Wall Street to (one hopes) a more normal state of affairs. It would be counterproductive to saddle financial institutions with punitive pay controls. But it would be equally mistaken to return to business as usual. With or without a nudge from government, Wall Street must learn and apply the lessons of the crisis. One of these is that compensation systems can provide employees with incentives to maximize short-term results -- and hence short-term income -- at the risk of giant, long-term losses. Kenneth R. Feinberg, the Treasury Department special master who oversees pay policy for bailed-out companies, has forced them to pay more compensation in long-term stock rather than bonus cash.

The Federal Deposit Insurance Corp., at the urging of Chairwoman Sheila Bair, has begun formal consideration of a proposal to link banks' deposit insurance fees' to their adoption of such payment rules. There are serious questions about whether the FDIC is the appropriate agency to spearhead such an effort. But the general idea that banks should be free to pay people as much as they want, as long as the method of payment is not financially destabilizing, makes sense. Boards of directors and shareholders must take a much more active role in ensuring sound pay policies. This is not only a matter of their own

interest but that of the public as well.

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'Acceptable to Feinberg'?

Charting a realistic future for executive compensation policy.

Tuesday, August 25, 2009

SHOULD CITIGROUP, which survives on tens of billions of dollars in U.S. government aid, pay energy trader Andrew J. Hall up to $100 million this year, as his contract arguably provides? That is the difficult question facing Kenneth Feinberg, the Treasury Department "special master" whose job is to ensure that compensation at bailed-out firms rewards talent without soaking the taxpayer. And Mr. Hall's pay is only one of many such hard cases; last Friday, firms such as General Motors and AIG submitted their executive compensation plans, hoping that they will prove "acceptable to Feinberg," as one official explained to the Wall Street Journal. We don't envy either the companies or Mr. Feinberg, but, when corporate compensation decisions affect taxpayer interests, government properly takes an interest in them.

Still, this state of exception will pass. It is not too soon to develop a post-crisis policy on executive compensation. If Citigroup were still entirely private, management could simply argue that the benefits of Mr. Hall's compensation package outweigh the risks -- including the risk that some other company might offer Mr. Hall a better deal -- and that, if not, the board will hold management accountable. The same theory applies to all executives: If they don't perform, the board cuts their pay or fires them. Alas, this model does not necessarily apply in an era of "board capture" by chief executives. Nor is it necessarily good for society when executives can structure their pay deals to reward short-term performance -- some measures of which, such as quarterly earnings, can be manipulated.

Believing that out-of-control executive compensation contributed to the financial meltdown, the House of Representatives recently passed the Corporate and Financial Institutions Compensation Fairness Act. Quite correctly, the bill tried to strengthen corporate governance. One of its means for doing that, however, a nonbinding shareholder vote on executive pay, might backfire if boards shape executive pay to please shareholders, who might be greedy for short-term profit themselves. More promisingly, the bill tries to ensure the independence of boards' compensation committees and the consultants who advise them. But it's maddeningly vague on defining that goal, as well as the goal of identifying, and banning, compensation that might destabilize the company or the economy.

Executive compensation is already covered by the law of unintended consequences. In 1993, Congress abolished the tax-deductibility of salaries over $1 million per year, except for "performance-based" pay. Stock options and other compensation linked to share prices proliferated, arguably exacerbating short-termism. Regulators imposed ever-more elaborate disclosure rules, which did little but make companies' regulatory filings unreadable.

The solution, if any, would follow several broad concepts: maximum vigilance by maximally empowered directors and shareholders; less governmental micromanagement and more loophole-free progressive taxation; less populism and more realism about what it takes to hire and retain world-class talent; and the speedy reprivatization of corporate America, so that executive pay can be depoliticized to the greatest possible degree.

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Bloomberg.com

Feinberg 'Concerned' Pay Cuts Could Drive Out Talent (Update3)

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By Ian Katz

Nov. 12 (Bloomberg) -- **Kenneth Feinberg**, the Obama administration's special master for executive compensation, said he is "very concerned" about the possibility his pay cuts may drive talent away from companies bailed out by U.S. taxpayers.

"I'm very cognizant of the concerns expressed by these companies," Feinberg said today in Washington at an event held by Bloomberg Ventures, a unit of Bloomberg LP, parent of Bloomberg News. "The law makes it clear that the determinations I render are designed, first and foremost, to make sure those companies thrive and that the taxpayers get their money back."

Feinberg has ordered pay cuts averaging 50 percent for the top 25 executives at **Citigroup Inc.**, Bank of **America Corp.**, American International Group Inc. and four other companies that took U.S. bailout money. He will rule on pay structures covering the next 75 highest-paid employees at those firms by year-end.

"Maybe I've struck the right balance," Feinberg said, referring to criticism that he has been too harsh and too easy on executives. "Hopefully some of this will percolate into the private sector, we'll have to see."

The U.S. will track possible executive defections by seeking from the seven companies data on comparative pay, by obtaining independent information and requesting "anecdotal evidence of vacancies and concerns about losing people," he said.

"You cannot help but be sensitive to the political realities," Feinberg said. "You can't have blinders on." He added that there was "no vindictiveness in my decisions. There's no revenge."

AIG'S Benmosche

Feinberg said AIG Chief Executive Officer **Robert Benmosche**, who took over the insurer in August, had "expressed his concern that compensation keep his people on board and that the company thrive." Feinberg told reporters he has met with the chief executive "one or two times over the last few months."

Benmosche yesterday wrote to AIG employees, saying he remains "totally committed" to leading the insurer after media reports suggested he told the board he may step down because U.S. pay caps hurt his ability to retain staff.

Benmosche released the letter after the Wall Street Journal said Nov. 10 that he told directors last week he might resign because of U.S. limits on employee compensation. Benmosche, who came out of retirement to lead New York-based AIG, said he is "frustrated" with limits on what the company can pay its top 100 executives.

Phibro Sale

Citigroup last month agreed to sell its Phibro LLC energy- trading unit to Occidental Petroleum Corp. to avoid a showdown with Feinberg over a proposed $100 million pay package for **Andrew Hall**, Phibro's chief executive officer.

"It was Citigroup that made the determination that it did not want Phibro and its traders to be subject to my jurisdiction," Feinberg said. "They made the voluntary decision to spin that unit off." Feinberg noted that he had "expressed reservations" that Hall's pay might constitute "excessive risk."

Phibro, based in Westport, Connecticut, made money in each fiscal year since 1997. New York-based Citigroup, which had a record $27.7 billion net loss last year, accepted a price of about $250 million, less than Phibro's average annual earnings.

Goldman Sachs Group Inc., Morgan Stanley and JPMorgan Chase & Co.'s investment bank, all exempt from Feinberg's oversight, will hand out a combined $29.7 billion in bonuses, according to analysts' estimates. That's up 60 percent from last year and more than the record $26.8 billion in 2007. The companies are the biggest banks to exit the Troubled Asset Relief Program.

To contact the reporter on this story: **Ian Katz** in Washington at **ikatz2@bloomberg.net**.

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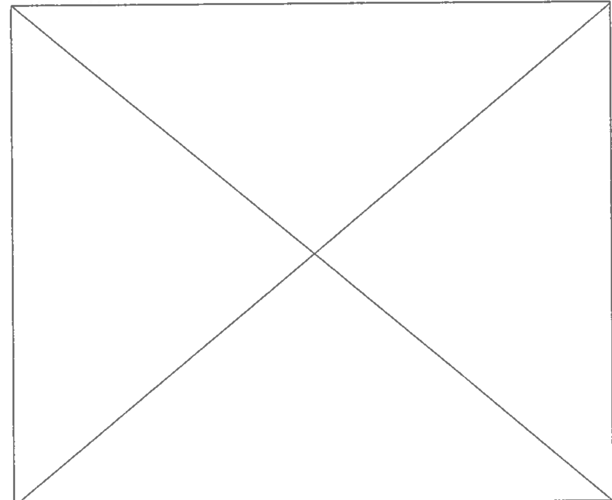
The Washington Post

Top employees leave financial firms ahead of pay cuts

Grass is greener where bonuses are sky-high



By Tomoeh Murakami Tse and Brady Dennis
Washington Post Staff Writer
Friday, October 23, 2009

NEW YORK -- Even before the Obama administration formally tightened executive compensation at bailed-out companies, the prospect of pay cuts had led some top employees to depart.

The administration had tasked Kenneth Feinberg, the Treasury Department's special master on compensation, to evaluate the pay packages of 25 of the most highly compensated executives at each of seven firms receiving exceptionally large amounts of taxpayer assistance.

But Thursday, he ruled only on slightly more than three quarters of the pay packages that were to be under his purview. The balance reflected executives who have left since he began his work in June or will be gone by the end of the year.

Many executives were driven away by the uncertainty of working for companies closely overseen by Washington, opting instead for firms not under the microscope, including competitors that have already returned the bailout funds to the government, according to executives and supervisors at the companies.

"There's no question people have left because of uncertainty of our ability to pay," said an executive at one of the affected firms. "It's a highly competitive market out there."

At Bank of America, for instance, only 14 of the 25 highly paid executives remained by the time Feinberg announced his decision. Under his plan, compensation for the most highly paid employees at the bank would be a maximum of $9.9 million. The bank had sought permission to pay as much as $21 million, according to Treasury Department documents.

At American International Group, only 13 people of the top 25 were still on hand for Feinberg's decision.

Feinberg did not detail how he plans to tackle the politically sensitive issue of nearly $200 million in bonuses due in March to employees at AIG Financial Products, the unit whose complex derivatives contracts led to the collapse of AIG last fall. Feinberg has urged the company to find a way to scale back the bonuses in hopes of preventing another round of public outrage.

In his written ruling Thursday, Feinberg noted that the firm had played a role "in the events necessitating

taxpayer intervention," and concluded that AIG Financial Products employees should be paid only what their base salaries were on Dec. 31, 2008. In addition, he said that he continues to urge company officials to recoup the bonus payments that some Financial Products employees pledged to repay earlier this spring but did not. Until that issue is resolved, he wrote, employees should receive no pay in addition to their base salaries.

That news drew scorn Thursday from employees at AIG Financial Products who said they had repeatedly offered to rework their pay arrangements but that Feinberg was unwilling to work with them.

"He has zero credibility with FP employees at this point," said one employee, who was not authorized to speak on the record. "It's a very demoralized workforce."

Several of the companies said they had already been making changes in their compensation plans to better link executive pay to performance and that their compensation committees had worked closely with Feinberg's team to come up with a final plan reflecting that principle.

"We've been going down that road," said Bob Stickler, a Bank of America spokesman. "This is really more of the same." But he also said that the ruling "does go pretty far and there are competitive issues we're worried about."

On Wall Street, reaction to Feinberg's ruling was swift, with some executives arguing that it will further handicap the most troubled firms by driving away top employees while making companies unwilling to promote rising stars for fear of bringing them to Feinberg's attention.

But Nomi Prins, a former Goldman Sachs employee, said Feinberg's rulings are unlikely to change the culture of bonuses on Wall Street.

"I don't think Wall Street is afraid of this at all," said Prins, author of "It Takes a Pillage: Behind the Bailouts, Bonuses, and Backroom Deals from Washington to Wall Street."

"It's going to affect a small portion of a small portion of the industry. It won't have a lasting impact."

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