

## Japanese Bankers Association

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May 31, 2011

Ref: CHC/6/H23

Board of Governors of the Federal Reserve System (FRB)  
20th Street and Constitution Avenue, NW.,  
Washington, DC 20551  
12 CFR Part 236  
[Docket No. R-1410]  
RIN 7100-AD69

Federal Deposit Insurance Corporation (FDIC)  
550 17th Street, NW., Washington, DC  
20429  
12 CFR Part 372  
RIN 3064-AD56

Office of the Comptroller of the Currency (OCC)  
250 E Street, SW., Mail Stop 2-3,  
Washington, DC 20219  
12 CFR Part 42  
[Docket No. OCC-2011-0001]  
RIN 1557-AD39

Office of Thrift Supervision (OTS)  
1700 G Street, NW., Washington, DC  
20552  
12 CFR Part 563h  
[Docket No. OTS-2011-0004]  
RIN 1550-AC49

National Credit Union Administration (NCUA)  
1775 Duke Street, Alexandria, Virginia  
22314-3428  
12 CFR Parts 741 and 751  
RIN 3133-AD88

Securities and Exchange Commission (SEC)  
100 F Street, NE., Washington, DC 20549  
17 CFR Part 248  
[Release No. 34-64140; File no. S7-12-11]  
RIN 3235-AL06

Federal Housing Finance Agency (FHFA)  
Fourth Floor, 1700 G Street, NW.,  
Washington, DC 20552  
12 CFR Part 1232  
RIN 2590-AA42

Re: Proposed Rulemaking on *Incentive-Based Compensation Arrangements*

Ladies and Gentlemen:

The Japanese Bankers Association (JBA) is an industry association of 140 Japanese banks and 46 non-Japanese banks with operations in Japan.

JBA appreciates the opportunity to comment on the Proposed Rule, *Incentive-Based Compensation Arrangements*, released March 30, 2011, by the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the Federal Housing Finance Agency (FHFA), the National Credit Union Administration (NCUA), the Office of the Comptroller of the Currency (OCC), the Office of Thrift Supervision (OTS),

and the Securities and Exchange Commission (SEC) (collectively, the Agencies).

The Proposed Rule currently applies to non-US banks operating within the United States. However, if such bank is subject to comprehensive consolidated supervision (CCS) by its home country regulator, as determined by the FRB, then the Proposed Rule should not be applied to such bank and deference should be given to such bank's home country regulator. Nonetheless, in the event that the Proposed Rule is ultimately applied to foreign banks operating in the US, some aspects are unclear regarding that application to foreign banks, including Japanese banks. We therefore believe that, in such event, those aspects should be clarified and that the Proposed Rule should be considered carefully in being applied to non-US banks.

We hope that our comments below will assist the Agencies in finalizing the Proposed Rule going forward.

(General Point)

○ Non-US banks with compensation practices regulated and monitored in their home countries should be exempted

The Proposed Rule would regulate non-US banks with operations within the US as *covered financial institutions*.

Japan has implemented new supervisory practices starting on March 4, 2010, based upon the Financial Stability Board's *Principles for Sound Compensation Practices* (April 2009) and the *Principles for Sound Compensation Practices—Implementation Standards* (September 2009).

Thus, the home country financial supervisory practices applicable to Japanese financial institutions that are subject to these regulations and monitoring in Japan should be given deference, and these financial institutions should be exempted from the Proposed Rule. So long as the prudential standards are consistent with international norms, Japan's application of its prudential standards to Japanese financial institutions should be respected by supervisors in other countries.

(Specific Points)<sup>1</sup>

1. Clarification of personnel covered by regulation (§236.3 (c), (d), etc. based on Regulation JJ, same below)

Under the current language in §236.3 of Regulation JJ, when the Rule applies to both (c) *covered financial institution* and (d) *covered person*, in the case of a foreign financial institution that is also a true bank holding company as defined in 12 CFR 225.2 (c), the Proposed Rule appears to also pertain to head office executive officers and employees.<sup>2</sup>

We assume that the apparent application of the Proposed Rule to all operations of financial institutions that are true bank holding companies is not the Agencies' intention. Therefore, we ask that the language be modified to clarify that in case of foreign financial institutions, the Proposed Rule applies only to executive officers and employees who are engaged in US operations, regardless of whether they are true or "deemed to be" bank holding companies

2. Clarification of subsidiary companies covered by regulation (Regulation JJ §236.3 (c), (d), etc.)

The current language in the Proposed Rule states that *a covered financial institution includes subsidiaries of the institution*. Consistent with the statutory language concerning *material financial loss* as defined in the Dodd-Frank Wall Street Reform and Consumer Protection Act, *subsidiaries* should be limited to material subsidiaries and subsidiaries comprising *major business lines* (see also *3. Clarification of executive officer covered* below).

Moreover, *covered financial institution* should be clarified to include subsidiaries on a consolidated basis for purposes of the regulation relating to material financial losses and reporting. For example, only the covered financial institution should submit required reports that include information

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<sup>1</sup> In the event that the Agencies are unwilling to accept the General Point above and exempt Japanese financial institutions from the application of the Proposed Rule, then we ask that the Agencies take into account the following specific points with regard to the application of the Proposed Rule to Japanese financial institutions.

<sup>2</sup> We note that the application of the Proposed Rule to foreign banks treated as bank holding companies under §8(a) of the International Banking Act of 1978 is limited to their US operations.

received from its subsidiaries; the subsidiaries themselves should not submit these reports directly to the regulators.

### 3. Clarification of *executive officer* covered (§236.2. 3 (f), etc.)

We think the term *head of a major business line* is broadly defined and needs further clarification. Consistent with the statutory language of Dodd-Frank concerning *material financial loss*, *head of a major business line* should be clarified to include only business lines which could produce a material financial loss for the covered financial institution on a consolidated basis (for which purpose changing *major business line* to *material business line* would be clearer).

Furthermore, it should be clarified that the term *executive officers* used in the proposed regulation does not apply to *executive officers* of those subsidiaries that are not (a) material subsidiaries, or (b) subsidiaries comprising *major business lines*. In the case of a subsidiary that includes a *major business line*, it should be clarified that the *head of a major business line* in the Proposed Rule applies only to the head of the major business line, and not to other group leaders or those who are in equivalent positions in the same subsidiary.

### 4. Clarifying the definition of *incentive-based compensation* (§236.2. 3 (g), etc.)

We believe the term *incentive-based compensation* is defined too broadly and needs further clarification.

For example, consistent with the Guidance issued in 2010 by the FRB, FDIC, OCC, and OTS, the term *incentive-based compensation* should mean only *that portion of an employee's current or potential compensation that is tied to achievement of one or more specific metrics (e.g., a level of sales, revenue, or income)*.

### 5. Introducing financial thresholds for covered incentive compensation (§236.2. 3 (g))

The Proposed Rule should be limited to total compensation that meets or exceeds a minimum threshold amount, and a specific financial threshold

should be defined (i.e., similar to the \$250,000 threshold under the Troubled Asset Relief Program (TARP)).

#### 6. Establishment of conformance periods

The evaluation periods for incentive-based compensation differ among financial institutions. Further, it is by nature difficult to change or modify incentive-based compensation plans during an evaluation period or retroactively. Also, existing employment contracts must be taken into account when changing incentive-based compensation arrangements.

Thus, adequate conformance periods should be established so that the covered financial institutions can shift to the new compensation requirements from the beginning of the fiscal year following publication of the final Rule.

#### 7. Introduction of a deferred compensation plan and safe harbor provision (§236.2. 5 (b) (3) (i), etc.)

Given the various compensation mechanisms, the Proposed Rule should provide guidance on determining and applying the 50% deferred compensation requirement.

Also, a safe harbor provision should be established for calculations that initially appear to be appropriate, but that later prove to be inappropriate for reasons unforeseen or otherwise out of the institution's control.

#### 8. Clarification of the definition of persons (other than executive officers) who individually have the ability to expose an institution to substantial losses (§236.2. 5 (b) (3) (ii) )

It should be clarified that the language *individually* in the phrase *covered persons (other than executive officers) who 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* means within the discretionary authority of the individual concerned.

#### 9. Arrangements for inter-Agency jurisdiction

The Proposed Rule does not establish procedures for regulatory oversight

when multiple Agencies have authority over a particular covered financial institution, such as when an FRB-registered large bank holding company owns an SEC-registered broker-dealer that is a covered financial institution.

We thus seek arrangements to be made among Agencies when multiple oversight Agencies are involved to ensure consistency and minimize unnecessary compliance burdens.

#### 10. Clarification of oversight authority regarding employees of financial institutions operating globally

Because the coverage of the Proposed Rule includes large US branches of non-US banks and non-US branches of US financial institutions, regulations may potentially conflict in regard to regulatory authority of incentive-based compensation of employees of financial institutions operating globally.

We request that the incentive-based compensation of employees of non-US financial institutions based temporarily outside their home country be regulated by home country regulators. If the intent of the Proposed Rule is to cover the incentive-based compensation of employees of US financial institutions who work outside the US, then we believe that the incentive-based compensation of employees of non-US financial institutions who work in the US should be regulated by their home country regulators.

#### 11. Clarification of approval procedures for *covered persons* employed by subsidiary companies (§236.2. 5 (b) (2) (ii), §236.2. 6, etc.

We think the Board of Directors of the relevant subsidiary company should determine and approve the incentive-based compensation practices of such subsidiary company when employees of such subsidiary company are *covered person(s)*.

The Proposed Rule appears to require that the incentive-based compensation practices be determined by the Board of Directors of the parent company. It should be clarified that this is not the case.

#### 12. Response of Agencies upon receipt of reports for regulatory authorities (§236.2. 4, etc.)

A timeframe should be established under which, once a covered financial

institution submits its annual report, the overseeing Agency must respond by accepting the report, rejecting the report as incomplete, or requiring revisions.

Given the extreme time sensitivity of incentive plans, Agencies should be required to respond within 30 days so that any corrections or changes can be made by the financial institution in a timely manner.

The rules should also recognize a safe harbor provision for the incentive-based compensation arrangements of the covered financial institution described in the report if the Agency does not respond within the given time period. In this way, the covered financial institution will be able to avoid a safe harbor not being recognized and therefore be exposed to unlimited liability.

Respectfully submitted,

Japanese Bankers Association