EXECUTIVE SUMMARY

The Federal Deposit Insurance Act ("FDI Act') allows the FDIC to limit or prohibit the payment of golden parachutes by troubled insured depository institutions and covered companies. Under the regulations, if such an entity is defined as "troubled" (*i.e.,* composite rating of 4 or 5, or meets other defined criteria), it cannot make, or agree to make, a golden parachute payment unless it is one of the three permissible golden parachute payments that may be made by a troubled entity with prior supervisory approval.

Certifications and Review Factors

This Financial Institution Letter ("FIL") supplements the rule and provides more detailed guidance regarding the type of information that will satisfy the certification requirements. Under the filing procedures, the applicant must demonstrate that: (1) the institution-affiliated party ("IAP") has not committed any fraudulent act or omission, or breach of trust or fiduciary duty or insider abuse, that has had a material adverse effect on the institution or covered company; (2) that the IAP is not "substantially responsible" for the insolvency or troubled condition of the institution or covered company; and (3) that the IAP has not violated any applicable federal or state banking law that has had or is likely to have a material effect on the institution or covered company. This FIL provides guidance about FDIC's expectations for the review process by which applicants arrive at this determination, particularly for IAPs who are senior management, directors, or otherwise have significant responsibilities. Accordingly, the application should also identify the responsibilities and specific areas of the bank that report to and are supervised by the IAP as well as major policy and operational programs initiated or managed by the IAP. Institutions should be aware that applications related to senior management will be evaluated both on the individual's performance as well as his or her influence and involvement over major corporate initiatives and policy decisions, especially any actions that may have facilitated high-risk banking strategies. As voting members of various Board committees, these executives can expect to be viewed as being accountable for those decisions.

Combined Applications Are Permitted

Combined applications are permitted in situations where the institution seeks to pay relatively small amounts to lower-level employees with similar responsibilities or to implement a reduction-in-force or reorganization and must terminate numerous employees to cut costs.

De Minimis Rule

The FDIC is implementing a *de minimis* payment amount of up to $5,000 per individual that will automatically be approved without requiring an official review. The bank is required to maintain a listing of the individuals who received these payments.

Precarious Financial Condition

The FDIC is unlikely to approve golden parachute payments for institutions that are in a precarious financial position, unless the institution can demonstrate near-term benefits that outweigh the cost of the payments and the payment is otherwise not contrary to the intent of the golden parachute restrictions.

GUIDANCE ON GOLDEN PARACHUTE APPLICATIONS

Purpose and Background

This guidance is intended to explain the golden parachute application process for troubled institutions and to instruct and advise bank management and supervisory personnel on the type of information that will be necessary to satisfy the requirements for applications by insured depository institutions and other covered companies seeking supervisory approval to enter into a contract to make, or to actually make, a golden parachute payment that is otherwise impermissible under existing law.

In 1990, Congress amended the Federal Deposit Insurance Act ("FDI Act") to provide that the FDIC may limit or prohibit the payment of golden parachutes by troubled insured depository institutions and covered companies. *See* 12 U.S.C. § 1828(k). The FDIC's implementing regulations provide that if such an entity is "troubled" (*i.e.*, has a composite rating of 4 or 5, or meets other defined criteria), it cannot make, or agree to make, a golden parachute payment except as provided by these rules.[1] *See* 12 C.F.R. Part 359.

As noted in the FDIC's original regulatory proposal, the purpose of the statute and regulations is to preclude institutions that are experiencing financial difficulty from making payments to institution-affiliated parties ("IAPs") that are not in the best interests of the institution, to protect institution assets from wrongful disposition, to provide the Corporation with tools to combat fraud and abuse, and to prevent payments that are inconsistent with or effectively at the expense of the Deposit Insurance Fund. *See e.g.*, 56 Fed. Reg. 50,529, 50,530 (Oct. 7, 1991). Consistent with the statute and its purposes, no golden parachute payment can be made unless permitted under the rules. The regulations set forth an express list of three "permissible golden parachute payments" that may be made by a troubled entity with prior supervisory approval.[2]

As the number of "troubled" institutions has risen, there has been a noteworthy increase in the number of applications seeking permission to make such golden parachute payments under the exceptions. Applicants seeking permission to make such payments must fully address the provisions of the golden parachute regulations and related application procedures to ensure the

[1] References herein to an entity being "troubled" is shorthand for those satisfying the conditions outlined under 12 C.F.R. § 359.1(f)(1)(ii)(A)-(E). The regulations prohibit both entering into agreements to make a golden parachute payment, or actually paying a golden parachute payment, except as permitted under the rules. Throughout this guidance, any reference to the covered entities' inability "to make" such a payment is intended to cover the inability to enter into an agreement to make such a payment as well. It is additionally worth noting that, notwithstanding prior supervisory approval being granted to a covered entity to *enter into an agreement* to make a golden parachute payment, supervisory approval is still needed for the entity to later actually *make* the payment.

[2] The rules specifically define certain severance payments that do not constitute "golden parachute payments," and thus are outside the scope of the rules. The restrictions do not apply to the payment of salaries or bonuses; instead, the restrictions apply solely to payments by troubled entities that are "contingent on termination," or that, by their terms, are explicitly payable on or after termination. Even so, certain kinds of payments are not restricted because they are excluded from the definition of "golden parachute." The excluded payments are the following (12 C.F.R. § 359.4(f)(2)): (1) payments pursuant to a qualified pension or retirement plan; (2) payments pursuant to an employee welfare benefit plan; (3) payments pursuant to a bona fide deferred compensation plan; (4) payments made by reason of death or disability; (5) payments pursuant to a "nondiscriminatory severance pay plan"; and (6) payments mandated by state or foreign law.

purposes of the law are met. There is also an expectation that these rules continue to be applied in a consistent manner. Consequently, the FDIC is providing this supervisory guidance to ensure that the original purposes of the statute and related rules are met.

Permissible Exceptions for Payments Otherwise Prohibited

There are three exceptions or "permissible" golden parachute payments by troubled entities: (1) those that receive the "regulator's concurrence"; (2) those for a "white knight" hired pursuant to an agreement to become an institution-affiliated party when the covered entity is "troubled" or to prevent it from imminently becoming so; and (3) those reasonable payments not to exceed 12 months' salary to an IAP in the event of a change in control (that does not result from an assisted transaction or from being placed in conservatorship or receivership). Each of these requires a written application and supervisory approval pursuant to 12 C.F.R. § 359.6.

The filing procedures, which are set forth under 12 C.F.R. § 303.244, address an applicant's need to provide certification and documentation as to each of the elements outlined under 12 C.F.R. § 359.4(a)(4) and described more fully below. These provisions require that an applicant specifically address whether it possesses or is aware of any information, documents, or other materials that would provide a reasonable basis to believe that the IAP has committed fraud, has violated the law, or is responsible for the institution's condition. The Corporation will weigh this information along with other factors when making a determination under 12 C.F.R. § 359.4(b).

Certification and Documentation Requirements

The Need for a Complete Application

In order to initiate supervisory review and approval, the applicant must submit a written application and provide necessary certifications with respect to each terminated IAP whom it seeks to pay under 12 CF.R. § 359.4(a)(4). When evaluating applications, a careful review of the required certification under 12 C.F.R. § 359.4(a)(4) is critical. If the certification and necessary supporting documents are not submitted, the application is deemed incomplete and cannot be processed. If sufficient information is not subsequently provided, then the incomplete application will be returned. It is, of course, vital for an applicant to address the factors identified under 12 C.F.R. § 303.244(c) (*e.g.*, reasons for the payment, identification of the IAP, copy of the agreement, etc.).

The Need to Address the Specific Certification Factors

In applying for approval to make the payment, the applicant should demonstrate that no reasonable basis exists to believe that: (1) the IAP has committed any fraudulent act or omission, or breach of trust or fiduciary duty or insider abuse, that has had or is likely to have "material adverse effect" on the institution or covered company; (2) that the IAP is "substantially responsible" for the insolvency or troubled condition of the institution or covered company; and (3) that the IAP has violated any applicable federal or state banking law that has had or is likely to have a material effect on the institution or covered company. The history of the FDIC's adoption of the golden parachute regulations indicates that it was not intended that an applicant be required to "prove the IAP's innocence." Rather, the applicant is expected to "demonstrate

that it does not possess and is not aware of any information, documents or other materials which would indicate that at the time the payment is proposed to be made there is a reasonable basis to believe" that the IAP's conduct falls within any of these enumerated scenarios. As discussed further in this Guidance, it will be insufficient for an applicant to solely provide a bare certification (*i.e*. not providing supporting documents or explanations) that the applicant "possesses no information giving [applicant] a reasonable basis to believe that any of the Section 359.4(a)(4)(i) through (iv) provisions is met."

Each IAP to whom the institution or covered company seeks to make a payment requires a certification. This certification must be prepared by an individual in a position, and with sufficient responsibility and access to information, to be able to provide a meaningful certification as to the substance of the Section 359.4(a)(4)(i) through (iv) provisions.

Information Required to Assess the Job Performance of IAPs with Significant Responsibilities.

Golden parachute payments pursuant to an employment or similar agreement most commonly involve IAPs with significant responsibilities. The certification should identify the responsibilities and specific areas of the bank that report to and are supervised by such IAPs. Major policy and operational programs initiated and/or managed by the IAP should be identified and briefly described. A performance assessment for the areas that report to the IAP, if applicable, should be included to indicate whether the area under his or her control improved or deteriorated during the time the IAP supervised the area. To the extent the IAP's work duties, responsibilities, areas of oversight, or those of his or her subordinates, fall within areas of the institution's operations that have been recently criticized in examination reports, visitations, or other formal or informal supervisory communications, more information is required. The certification should address and reflect consideration of this criticism, and the applicant should concisely explain on what basis the applicant concluded there was insufficient information to provide a reasonable basis to conclude that the IAP is substantially responsible for the institution's or covered company's troubled condition. Simply put, the certification should address recent, relevant criticism by supervisory authorities and otherwise describe the review process supporting the conclusions in the certification.

The above is not intended to be an exclusive list of information or items to be addressed, as additional information may be needed or more issues may need to be addressed. At a minimum, a complete application is one that reflects sufficient overall information to assess the reasons for, and costs and impacts of, the proposed payment in order to support supervisory approval. Unless and until the applicant provides information and documents to meet this certification requirement -- which the Corporation or other federal regulator staff may require in follow-up correspondence -- the application will not be considered complete.

The purpose of this requirement is to provide the Corporation with sufficient meaningful, and common-sense information to be assured that the purposes of the Section 1828(k) restriction are being met (*i.e.*, to protect institution's and covered company's assets from wrongful disposition, to combat fraud and abuse, and to prevent payments that are inconsistent with the institution's best interests and ultimately at the cost of the Deposit Insurance Fund). For instance, assume an institution is in troubled condition due in significant part to identified weaknesses in its commercial lending function. In such an instance, merely providing a bare certification that the institution "does not possess and is not aware of any information, documents or other materials which would indicate that at the time the payment is proposed to be

made there is a reasonable basis to believe" that the IAP is substantially responsible for the institution's troubled condition -- when such IAP in fact has significant supervisory oversight with respect to the commercial lending function -- is an incomplete certification. Another example might include an IAP that failed to properly respond to internal or external audit reports that highlighted significant internal control weaknesses, which ultimately resulted in substantial losses. In both examples, additional supporting information would be appropriate.

The Rules Allow Flexibility for Certain Golden Parachute Payments

Concern has been raised as to the ability of the golden parachute rule, and the certification and documentation requirements in particular, to provide adequate latitude for an institution to pay relatively small amounts to lower-level employees, or to address situations where the institution seeks to implement a reduction in force or reorganization and must terminate numerous employees over a short period of time. It has been suggested that, in such instances, the rule's application and documentation requirements can operate to delay and unnecessarily complicate such efforts, particularly when the sums involved are relatively small and the employees are not executive-level. The existing rule reflects the tension between the competing concerns of trying to ensure that payments are not made to individuals who have engaged in acts detrimental to an institution, while allowing institutions sufficient latitude to implement needed personnel planning and downsizing that can be facilitated by the payment of severance.

The nondiscriminatory severance pay plan exception under § 359.1(f)(2) was introduced to address, in part, broad-based efforts by an institution to provide severance for large groups of employees. The regulatory history of this provision clearly indicates that this provision was intended to include a range of circumstances, including reduction-in-force circumstances. Although this exception has been criticized as being overly narrow and difficult to meet, the rule's definition of "nondiscriminatory" reflects that the exception was not intended to allow institutions to provide greatly different severance amounts to different groups of employees. Too broad an exception, in other words, could easily be misused as a method for troubled institutions to pay excessive severance to some small number of employees, to the detriment of other employees, the institution, and potentially the Deposit Insurance Fund.

In order to provide some flexibility, this Guidance incorporates a *de minimis* golden parachute payment provision, as described below, which should assist in permitting institutions to pay relatively small amounts without seeking supervisory review. In fact, the amount of this *de minimis* provision has been set in a manner expected to have an appreciable effect, based on supervisory experience. Second, it should be emphasized that the golden parachute application process *does* allow an institution to file a golden parachute application on behalf of numerous employees in one combined application. For instance, in a reduction-in-force situation, a troubled institution could file one application seeking to make a payment to twenty tellers under a restructuring plan seeking to close several branches, or another application seeking to terminate twenty loan processors due to adverse conditions in the housing market.

Combined Applications that Address Regulatory Requirements are Permitted

In reviewing such a "combined application," supervisory staff must seek to discern that the payments being made to a category of employees are not greatly disparate, that the type of employees (their positions) in a particular category are not vastly different, and that the range of payments, while it may differ from one employee to another, is not appreciably different within the category. Importantly, supervisory staff must seek to ensure that a joint application on behalf of numerous employees is not being used as a means to "end-run" the rule's basic purposes. For example, in an application seeking to make golden parachute payments to twenty loan processors and customer service representatives ranging in amounts from $7,000-to-$9,000, the applicant should not also include a request to pay a senior loan officer a $60,000 golden parachute payment. In such circumstances, supervisory staff may require the filing of a separate application, with more detailed analytical support addressing the senior loan officer's responsibility, if any, for the institution's condition as well as the substance of the other Section 359.4(a)(4)(i) through (iv) matters.

In reviewing a combined application, supervisory staff must ensure that the institution has provided a certification that is meaningful with respect to the identified employees. While the rule envisions that each IAP to whom the institution or covered company seeks to make a payment requires a separate certification, the broad certification can suffice if it is substantive and complete, and has been prepared by an individual in a position, and with sufficient responsibility and access to information, to be able to provide a meaningful and accurate certification as to the substance of the Section 359.4(a)(4)(i) through (iv) provisions *with respect to each* of the employees in the combined application.

The content and breadth of a combined application will necessitate differing levels of detail, depending upon the specific factual circumstances. For instance, a meaningful application and certification may need to provide supervisory staff with not merely a description of the IAPs' job titles, but information as to the employees' basic duties if not self evident. The applicant must satisfy itself that the Section 359.4(a)(4)(i) through (iv) provisions have been carefully considered with respect to each listed employee. The applicant should review records and conduct sufficient research to conclude that, due to the nature of the functions and duties of the IAPs so listed, each is unlikely to have had a material adverse effect on the institution or to have substantial responsibility for the institution's troubled condition.

In reviewing such a combined application, supervisory staff may approve or deny some or all of the listed employees, may request additional information necessary to evaluate the application, or may require the institution to separate one or more employees from the combined application and direct an individual application for such employee(s). Senior executive officers, employees with specific severance agreements, and any other employee that, because of his or her job duties and responsibilities, could be reasonably expected to materially affect the direction or the condition of the institution, should not be submitted as part of a combined application. While the determination to file a combined application is subject to an institution's discretion, institutions must employ common-sense and reasonable criteria to ensure that employees with significant job responsibilities are not comingled with other lower-level employees on a single application.

This outlined information and review reflects that supervisory consideration of golden parachute applications is more substantive than merely considering a one-sentence certification. Still, this expectation and review is needed for the types of information that the FDIC has identified for those golden parachute applications for which FDIC consent is required.[3]

Senior Executive Officers

Senior executive officers and other executives identified as having significant influence over major corporate initiatives and policy decisions can logically be expected to have greater difficulty meeting the requirements under 12 C.F.R. § 359.4(a) and obtaining a favorable determination under 12 C.F.R. §359.4(b). For instance, if the executive is considered to be part of the senior management team and endorses a high-risk banking strategy as a voting member of the executive or similarly constituted board committee, and this strategy is substantially responsible for the entity's troubled condition, the application materials certainly must explain how this executive is not substantially responsible for the institution's condition. In such cases, merely asserting that the strategy "did not directly involve the executive's area of responsibility" is insufficient.

Factors Considered by Supervisory Staff in Weighing Completed Applications

After the required certification information under Section 359.4(a)(4) has been provided and is deemed complete, supervisory staff must weigh the application requesting an exception. Significantly, the fact that the applicant has made the required certifications does not *entitle* the applicant to approval. In short, the determination to be made is discretionary with the Corporation and/or federal banking regulator under the law. Supervisory staff may conclude, notwithstanding the applicant's certification, that the IAP is substantially responsible for the institution's condition. Alternatively, staff may simply conclude that, even if the IAP is not so responsible, the payment may be imprudent for one, or several, other reason(s). Specifically, as expressly provided in the rules, and consistent with the statute, in deciding whether to approve the golden parachute the primary regulator and the FDIC may consider the following:

- The degree of the IAP's "managerial or fiduciary responsibility"
- The length of the IAP's affiliation with the bank and the degree in which the payment represents "reasonable payment for the services rendered over a period of employment"
- Any other factors or circumstances that would indicate the payment would be contrary to the intent of the golden parachute restrictions.

In order to weigh such factors, supervisory staff requires information as to the IAP's responsibilities, the services the IAP has rendered, information as to his or her compensation history, the IAP's length of employment, and other information. For example, supervisory staff must be able to assess the employee's: area(s) of primary oversight and responsibility; major initiatives instituted by the employee, including a summary of the results; or areas where the

[3] *See* 12 C.F.R. § 303.244(c), (d) (outlining that the content clearly needs to address reasons, provide identification as to the recipient, provide information regarding any contract or agreement, address the costs and impact of such payment on the institution, provide reasons why the consent should be granted, address the certification and documentation issues in the Section 359.4(a)(4)(i) through (iv) provisions, and additionally citing the ability to request additional information at any time).

employee demonstrated strong leadership abilities or where this leadership resulted in positive or negative financial results.

Some overall assessment of the employee's performance should be included in the application to help determine whether the operations of the department and/or the bank improved or deteriorated during the time the employee was responsible for that area of the bank. Without such information or summary information, supervisory staff is unable to assess the above factors. In other words, in order to weigh whether it is in the interests of the institution or the Deposit Insurance Fund for a troubled institution to be providing an IAP with an otherwise prohibited golden parachute payment, it is helpful to understand whether employee's performance was weak, or the employee's actions were incidental to or linked to the bank's negative performance or historical areas of weakness. Moreover, even with respect to employees whose employment has had positive impact on the institution, to the extent such employees have been well- or adequately-compensated, or previously afforded incentive compensation for such services, the payment of a golden parachute for such already-compensated performance must be questioned.

Under the rules, both the Corporation and primary federal regulators may consider these factors, as well as other information pertaining to the intent and purposes of the Section 1828(k) rules. Supervisory staff should certainly question, and seek additional information about, applications where the requested payment falls outside the amount provided for employees with similar levels of responsibility and history for institutions or covered companies in the applicant's peer group. Moreover, such analysis should always be made within the context that the institution in question is in a troubled condition and such payments are otherwise not permitted. For example, if a similarly situated executive, with similar history and responsibility, at an institution within the applicant's peer group, is afforded 12 months' salary as a golden parachute payment, such information is relevant, but certainly not determinative where the application and IAP in question involve a troubled institution. In short, the fact that non-troubled entities make such payments does not dictate that a troubled institution should presumptively be allowed to do so, as the statute's intent clearly suggests otherwise.

In deciding whether to approve an otherwise impermissible golden parachute payment, and in weighing the factors described above, supervisory staff should distinguish between (1) cases in which no payment (in any amount) would be appropriate; and (2) cases in which a payment might be appropriate, but not in the amount specified in the application. The amount of a golden parachute payment must be weighed in the context of the insured depository institution's condition. Factors can include the size of the institution and the amount of the payment relative to its possible impact on the institution's capital and condition, the number of such payments the institution has made or seeks to make to other IAPs, as well as other factors such as how well the institution or applicant has demonstrated that the payment is reasonable in amount under the circumstances.

Deferred or Staged Dispersal Payments

All golden parachute applications are reviewed based on the certification and other information available at the time of the application. In some instances, information may later become available that would have led to supervisory disapproval of golden parachute payments. Supervisory staff needs to ensure that the institution and its successors expressly reserve the right to suspend or deny full allocation of all payments should later information warrant such action.

In determining whether to approve the application, supervisory staff should check whether the agreement provides for a staged dispersal of payments or provides that the institution or its successors retain the legal right to demand the return of any golden parachute payments made thereunder should the institution or its successors later obtain information indicating the IAP has committed, is substantially responsible for, or has violated, the respective acts or omissions, conditions, or offenses outlined under 12 C.F.R. 359.4(a)(4). If the agreement includes no such provisions (and the parties are unwilling to add any such provisions), the application generally should be disapproved. In addition, supervisory staff should require the agreement to contain a clause expressly conditioning the actual golden parachute payment on the institution or IAP having obtained necessary approvals from the applicant's primary federal banking regulator and/or the FDIC.[4] Such measures enabling the institution to suspend, prevent, or claw back some or all payments to an IAP, when warranted, will ensure that payments contrary to the intent of Section 18(k) of the statute are not made. *See* 12 U.S.C. § 1828(k); 12 C.F.R. § 359.4(b)(3).

Specific Exceptions: Regulator's Concurrence Exception

With respect to the "regulator's concurrence" approval under 12 C.F.R. § 359.4(a)(1), the specific circumstances when this exception is appropriate are not defined in the rules. The consent of both the primary regulator and the Corporation is necessary.

This provision was intended to be, and must be, narrowly construed. Historical application information, however, suggests that this exception is currently being used somewhat liberally to permit golden parachute payments. As a general proposition, this exception should not be viewed as being intended to permit golden parachute payments in excess of 12 months' salary for an IAP. For instance, the other permissible exception for changes in control is limited to 12 months' salary. *See, e.g.*, 12 C.F.R. § 359.4(a)(3). The rule itself suggests that the regulator's concurrence provision was intended, for instance, to potentially permit payments in excess of 12 months for nondiscriminatory severance plan payments. *See, e.g.*, 12 C.F.R. § 359.1(f)(2)(v).[5] The regulation's rulemaking history indicates that it could potentially allow a request for an exception in a case where a low-level employee may have a golden parachute agreement (expected to be a rare instance) and allow a request where an institution is deemed troubled only on account of being subject to a written supervisory agreement but is not experiencing significant financial difficulty. *See* 60 Fed. Reg. 16069, 16074, 16075 (March 9, 1995). This regulatory history does not suggest broad latitude to approve golden parachute agreements allowing payments in excess of 12 months' salary.

[4] As a matter of best practice, all insured depository institutions and other covered companies, regardless of their financial health, should add to their employment agreements a clause conditioning the payment of any severance benefits on compliance with applicable law, including 12 C.F.R. Part 359.

[5] The regulations specifically exclude from the definition of a "golden parachute payment" payments under a "nondiscriminatory severance payment plan" that meets specific parameters. 12 C.F.R. § 359.1(f)(2)(v). The nondiscriminatory severance payments excluded must not exceed the base compensation paid to the IAP during the 12 month period preceding termination. Also, the severance plan cannot have been adopted, or modified to increase the amount or scope of benefits, at a time when the entity was troubled. *However*, if the entity seeks to make a payment in excess of 12 months, it must receive the FDIC's approval (and not that of the appropriate federal banking agency). *Moreover*, if the entity seeks to increase or modify the amount of benefits either through adoption or modification at a time when it is troubled, the appropriate federal banking agency must consent (FDIC consent not required). *See* 12 C.F.R. § 359.1(f)(2)(v).

Permissible Exception for Changes in Control

With respect to the "change in control" approval under 12 C.F.R. § 359.4(a)(3), any payment requires that there be a change in control, that the payment be limited to 12 months' salary, and that the change in control cannot result from an assisted transaction or from being placed in conservatorship or receivership. Consent from the entity's primary regulator is necessary, but no FDIC consent is necessary (unless the Corporation is the primary regulator).

This exception is provided in recognition of the fact that, in order to keep current management of a troubled institution sufficiently motivated while seeking out potential acquirers -- an acquisition that could, potentially, result in such management employees being put out of work -- some golden parachute payments are in fact consistent with the statute's purposes. In short, a successful acquisition can be in the institution's best interests even when not in the best interests of the institution employees who may be facilitating it or specifically affected by it.

In conducting a review of institution requests to enter into agreements permitting change-in-control golden parachute payments, supervisory staff should question the institution or covered company as to why the agreement is needed as to a particular employee, and whether the institution has carefully considered the need to agree to provide such change-in-control payments in instances where the employee may be unaffected by the change. If an actual change in control is being negotiated, with the support of the appropriate federal regulator, supervisory staff should question whether the proposed change-in-control payments will be necessary or at least helpful in facilitating the change in control.

Permissible Exception for "White Knight" Employees

The third permissible exception is for golden parachute payments for a "white knight" hired pursuant to an agreement to become an IAP when the covered entity is "troubled" or to prevent it from imminently becoming so. 12 C.F.R. § 359.4(a)(2). The consent of the Corporation and the primary federal regulator is required.

Supervisory staff should ensure that the IAP/white knight to whom the covered entity seeks to make the payment must have been brought in from outside (*i.e.*, an existing employee of the institution cannot qualify as a white knight). The current regulations do not place a duration limit on such white knight arrangements. Theoretically, these arrangements are intended to provide incentive to a successful executive to leave a thriving business concern and assist in bringing a financial institution from troubled condition to one of greater financial stability. However, the longer a white knight remains at the financial institution, the less need there is, arguably, for the payment of a golden parachute should the white knight seek to leave the troubled institution.

Thus, while a white knight may justifiably require a golden parachute in recognition for having left a successful business and in recognition of the fact that he or she potentially might be unemployed should he or she be unable to turn-around a troubled institution and it fails soon thereafter, these justifications lose their persuasiveness as significant time passes. Existing regulations do not impose a years-limit on the duration of such agreements, nor on the payment of golden parachutes under them. However, in reviewing applications to approve an *agreement*, supervisory staff should inquire whether the institution considered the possibility of imposing a

years-limit (*e.g.*, possibly five years) on the duration of the golden parachute payment under such a provision, subject to the particular circumstances of the institution and market conditions.

Other Situations

Precarious Financial Condition

Throughout the application process, the FDIC will monitor the ongoing financial condition of the troubled insured depository institution or other covered company seeking approval to make a golden parachute payment. The FDIC is unlikely to approve golden parachute payments for institutions that are in a precarious financial position, unless the institution can demonstrate near-term benefits that outweigh the cost of the payments and the payment is otherwise not contrary to the intent of Section 1828(k). An insured depository institution would be considered to be in a precarious financial condition if its Prompt Corrective Action ("PCA") capital category under 12 C.F.R. § 325.103 is "significantly undercapitalized" or "critically undercapitalized." However, other institutions in higher capital categories or other covered companies that are not subject to the PCA regime may also be considered to be in a precarious financial condition.

De Minimis Rule

Over the past two years, there has been a significant increase in the number of relatively small golden parachute applications for employees and lower level managers that are subject to the same type of review and processing as the larger more complex applications. Thus, it has been necessary to assess the overall cost for processing these small payment amounts against the potential risk of loss, and the overall purposes of the rule and its restrictions. Specifically, supervisory staff has weighed the particularly low likelihood that certain low-dollar payments could be received by any individuals likely to fall within the parameters of the 12 C.F.R. § 359.4(a)(4) provisions seeking to preclude payments to IAPs who have committed any fraudulent act or breaches of fiduciary duty likely to have "material adverse effect" on the institution, or who may be "substantially responsible" for the insolvency or troubled condition of the institution or covered company. Having done so, the FDIC will, going forward, employ a *de minimis* payment of up to $5,000 per individual that would automatically be approved without requiring an official review. The only requirements are that the paying bank or covered company maintains at the institution written records of the individuals receiving the *de minimis* golden parachute payments, the dates and amounts of the payments, and a signed and dated certification. This certification must be executed prior to the payment being made. As additional *de minimis* payments are made over time new certifications will be necessary. All certifications must indicate that the preparer has no reasonable basis to believe the *de minimis* payment being made at that specific time is to an individual or individuals for whom the institution would be unable to make the certification as to the factors under Section 359.4(a)(4)(i) through (iv) if an application were filed for the individual. All certifications must be prepared and signed by an individual with sufficient responsibility and access to information to provide a meaningful certification. All certifications must be executed prior to the bank making the payments.

Although a higher *de minimis* limit would certainly provide greater relief and permit more golden parachute payments without an application, recent payment data reviewed by FDIC staff suggests that the median golden parachute payment is not greatly in excess of this $5,000

limit, and thus this *de minimis* threshold is expected to have meaningful effect while preserving supervisory review of the types of payments intended to be covered by the prohibition.

An insured depository institution whose PCA capital category is "significantly undercapitalized" or "critically undercapitalized" may not rely on the relief for *de minimis* golden parachute payments. Such institutions desiring to make golden parachute payments must obtain appropriate regulatory approval.

Salary Gross-ups and Other Similar Tax Payment Schemes

The FDIC does not condone and will not approve any payment that includes additional funding to the base salary for the purpose of paying the tax liability of the executive receiving the funds.