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Implications of the AIG Bonus Imbroglio

New York
March 29, 2009

Great outrage and indignation have been expressed, from multiple perspectives, in connection with AIG's retention bonuses and the Congressional response thereto. Now that most of the public, albeit probably not the actual participants, seem to be past the initial burst of emotion, we believe that it is well worth noting that *all* employers, whether or not they are recipients of Government funds, should pay close attention to the several recently proposed (and competing) bills in Congress spawned by the episode.

These bills show that the politics of populist furor over executive compensation can easily pave the way for hasty and thoughtless regulation, which would (if enacted as written) be counterproductive to the US financial system and economic recovery. The bills also foreshadow possible future and potentially broad legislation that may eventually have negative effects for many companies beyond the financial industry.

Political focus on, and accompanying rhetoric regarding, perceived excesses in executive compensation have been building in intensity for some time. The current legislative impulses, however, raise systemic risks that pose a far greater danger than the issues sought to be addressed by them. On March 19, 2009, the House of Representatives approved a bill to tax bonuses paid to employees of certain recipients of Troubled Assets Relief Program ("TARP")[1] funds at a 90 percent tax rate (H.R. 1586). H.R. 1586 was introduced in and approved by the House in a matter of days following the announcement of the bonuses paid to AIG executives.[2] The long-term dangers inherent in the Government dictating details of private sector pay practices and retroactively invalidating binding contracts through confiscatory taxing of a targeted group are obvious to most, and should be to all.[3]

[1] Troubled Assets Relief Program of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5221) ("EESA").

[2] A similar bill with an excise tax on bonuses of 35% payable by the employee and 35% payable by the employer was proposed in the Senate (S. 651) as described below.

[3] The Wall Street Journal, on March 20, 2009, reported on President Obama's appearance on "The Tonight Show with Jay Leno" and the President's reaction to H.R. 1586. The article states that:

The recent fit of public and legislative hysteria could provide a ready springboard for much broader-based executive compensation regulation proposals. The New York Times recently reported that "[t]he Obama administration will call for increased oversight of executive pay at all banks, Wall Street firms and possibly other companies as part of a sweeping plan to overhaul financial regulation, government officials said." On the same day, in an interview on CBS News' "Face the Nation," Congressman Barney Frank discussed the pending legislative measures and stated "also what's important for us . . . [is to] address the whole question of executive compensation and the perverse incentives you get from the way it's structured," which he noted he has "been trying to do . . . frankly since 2006." The American Recovery and Reinvestment Act of 2009 ("ARRA") added a "say on pay" requirement for all TARP participants,[4] which certain members of Congress, including Congressman Frank and then Senator Obama, have been advocating as a reform for public companies generally for some time, and a recently proposed Senate tax bill (S. 651) reprises a 2007 legislative proposal to limit deferred compensation generally to $1 million per year.[5]

A particularly troublesome aspect of the four recently proposed bills – the House tax bill (H.R. 1586), the Senate tax bill (S. 651), H.R. 1664 (adding additional executive compensation limitations to ARRA) and H.R. 1575 (authorizing the Attorney General to recover and limit excess compensation) – is the lack of an exception for existing binding compensation contracts. While the Obama administration has in its rules tried to honor existing agreements (including the ones between the Government and the institutions),[6] and while the provision in ARRA limiting incentive compensation to no more than one-third of total compensation has an exception for binding contracts in existence prior to its enactment,[7] the four recent proposals have no such exception. In fact, H.R. 1664 would specifically reverse ARRA's grandfather clause for TARP recipients' contractual

Mr. Leno was even more negative to the House plan, saying it "kind of scared me." "If the government decides they don't like a guy, all of the sudden hey we're going to tax you, and, boom, and it passes, that's *[sic]* seems a little scary," he said. "It was frightening to me as an American that Congress or whoever could decide I don't like that group, let's pass a law and tax them 90 percent."

[4] EESA § 111(f).

[5] Section 214 of Senate bill 349 (the "Small Business and Work Opportunity Act of 2007"), introduced to the Senate Finance Committee on January 22, 2007 by Congressman Baucus.

[6] The Treasury Department's enhanced conditions on executive compensation for companies receiving Government assistance would not "apply retroactively to existing investments or to programs already announced…." White House, Office of the Press Secretary, "Treasury Announces New Restrictions On Executive Compensation" (Feb. 4, 2009).

[7] EESA § 111(b)(3)(D)(iii).

arrangements, and H.R. 1575 would give the Attorney General express authority to review existing employment contracts, seek recovery of amounts paid under such contracts and limit the amounts that can be paid under such contracts following enactment.

One of the arguments raised for disregarding such contracts is made explicit in H.R. 1575, which authorizes the Attorney General to recover certain payments made by a company if such company would have been insolvent on the date of the payment were it not for the Government's injection of funds. In the bankruptcy context, of course, *pre-existing contracts* may be assumed or rejected post-filing, and there are well-established precedents and procedures for making judgments about whether assumption or rejection of particular contracts is in the best interests of the particular bankruptcy estate. Moreover, companies that enter bankruptcy often are permitted by the courts and creditors to adopt *new* incentive agreements with retention features. The analogy to the bankruptcy context is arguably relevant for considering whether executive contracts entered into by some TARP participants should be respected, and we believe that the analogy suggests careful consideration of specific facts and circumstances. However, many companies that participate in TARP were not, and were not expected to become, insolvent, and the analogy to the bankruptcy context for them seems inapt. Invalidating existing contracts for executives of those entities on a wholesale basis through blanket legislation seems plainly unwarranted.

It is similarly relevant to note that the Government's intervention in compensation of employees during times of serious economic stress is not unprecedented. Wage (and price) controls were implemented during World War II in an effort to stimulate the US economy, and again in the early 1970s in an effort to curb rampant inflation. However, unlike those measures, which applied on a national, economy-wide basis, the currently proposed legislation targets a specific group of companies and individuals perceived by many to be responsible, at least in part, for the current state of the national economy. In the circumstances, we believe that there is more than enough blame to go around to a wide group of businesses, Governmental authorities and individuals.

Moreover, unlike most previous executive compensation legislation (including TARP, even as amended by ARRA), the four recent proposals inequitably and unnecessarily reach employees far beyond the executive level. The bonus tax bills (H.R. 1586 and S. 651) by their terms could apply to a large number of employees of the affected institutions; H.R. 1664 and H.R. 1575 appear to apply to every single employee of the affected financial institutions. Following the precedent set by Senator Dodd's compensation restrictions set out in ARRA, the French government announced on March 24, 2009 that it also would issue a decree to limit stock options and bonuses for "executives" at firms that have received state aid. Unlike the pending proposals in the US to expand the scope of the executive compensation restrictions, the French proposal seems to be limited to executives.

Therefore, as executive compensation legislation has many times in the past, we believe that the legislation already enacted and the recent proposals may well have unintended and negative consequences to employers, employees and the public alike. Experience suggests that the legislation already enacted and that recently proposed should be expected to:

- Result in a significant loss of talent by institutions that are subject to compensation restrictions, with a shorter-term negative effect on each institution's ability to compete with unrestricted entities and to preserve the funds advanced by the Government as an investment, and with a longer-term negative effect on the institution's ability to preserve jobs and contribute tax revenues to all levels of Government. Lest one wonder whether executives considering a change of employment will be able to find better offers, it is noteworthy that H.R. 1664, in its current form, would have Treasury consult with the Chairperson of the Congressional Oversight Panel established under EESA (a panel of five, including the Associate General Counsel of the AFL-CIO) in setting standards for the reasonableness of executive compensation, and that, in addition to hedge funds and other non-bank financial institutions, many substantial non-US financial institutions will not be subject to the same pay restrictions as TARP recipients.

- Cause many TARP recipients to repay TARP obligations as soon as they can, negating the very goals of providing stability to the financial system and easing the credit market that caused TARP to be adopted in the first place.

- Deter any institution from seeking to participate in future economic recovery efforts because of the now demonstrated risk that Congress will change the rules of the game in the second quarter. The issue now is executive compensation, but the next issue could be windfall profits, in which case we may expect to hear shrill calls for a confiscatory retroactive tax on gains recognized by a private enterprise that decides to participate in the recently announced public-private partnership for the purchase of toxic assets held by financial institutions.

Forewarned is forearmed. Whatever the immediate prospects for passage may be, we believe that it is important for employers and employees generally to be aware of the substance of the recent proposals even if they are not the targets at the moment. Following is a brief summary of the executive compensation provisions of:

- American Recovery and Reinvestment Act, which is currently in effect (Appendix A);
- H.R. 1586, which was approved by the House on March 19, 2009 (Appendix B);

- S. 651 ("Compensation Fairness Act of 2009"), which was placed on the Senate Legislative Calendar on March 19, 2009 (Appendix C);
- ARRA as proposed to be amended by H.R. 1664, which was passed by the House Committee on Financial Services on March 25, 2009 (Appendix D) (changes proposed by H.R. 1664 appear in underlined text); and
- H.R. 1575 (the "End Government Reimbursement of Excessive Executive Disbursements (End GREED) Act"), which was reported by the House Committee on the Judiciary on March 24, 2009 (Appendix E).

As noted above, two of the four bills identified above (H.R. 1586 and S. 651) are primarily tax legislation. The other two bills (H.R. 1664 and H.R. 1575) take different approaches to controlling compensation practices, and could prove even more troubling than the proposed tax legislation in terms of their potential effect on non-TARP participant companies.

American Recovery and Reinvestment Act

The executive compensation related provisions of ARRA are summarized in our February 16, 2009 memorandum entitled "Overview of the Executive Compensation Provisions of the American Recovery and Reinvestment Act of 2009" (Appendix F).

H.R. 1586

- Imposes income tax on bonuses paid on or after January 1, 2009 to employees or former employees of covered TARP recipients at a rate of 90% of the lesser of: (1) the bonus amounts paid to such individual or (2) the amount of the individual's adjusted gross income exceeding $250,000 ($125,000 in the case of a married individual filing a separate return). This tax is imposed in lieu of ordinary income tax on the bonus.
    - Covers retention payments, incentive payments and all other bonuses that are in addition to amounts payable at a regular periodic rate for services performed. Excludes commissions, welfare and fringe benefits and expense reimbursements, but includes any employer reimbursement for tax imposed under this legislation.

- Tax is not imposed on any amount which the employee irrevocably waives or returns to the TARP recipient before the close of the taxable year in which such payment is due, provided the employee does not receive any benefit from the employer in connection with the waiver or return.

- Defines "covered TARP recipient" to include: (1) entities that received capital infusions under EESA in the aggregate exceeding $5 billion and their affiliates; (2) Fannie Mae, Freddie Mac and their affiliates; and (3) any partnership if more than 50% of the capital or profits interests of the partnership are owned (directly or indirectly) by entities described in clauses (1) and (2).
    - An entity that received funds under EESA is no longer a covered TARP recipient if it repays its outstanding TARP amounts that exceed the $5 billion threshold.

S. 651 ("Compensation Fairness Act of 2009")

Tax on Excessive Bonuses

- Imposes a 70% excise tax (35% payable by the employer and 35% payable by the employee) on any "excessive bonus" paid on or after January 1, 2009. This excise tax is in addition to the employee's regular income tax on the bonus.
    - Covers all officers, directors and employees, regardless of income. Does not expressly cover former employees. Expressly covers foreign employees.
        - If the excise tax cannot be collected from a foreign employee, the employer must pay the employee's share of the excise tax.
    - Covers employers that are (1) entities in which the Federal government acquires capital investments under EESA or Section 13 of the Federal Reserve Act in the aggregate exceeding $100 million and their affiliates and (2) Fannie Mae, Freddie Mac and their affiliates.
        - An entity described in clause (1) is no longer covered if it repays its outstanding TARP amounts that exceed the $100 million threshold.
        - Provides for a waiver on any restriction or prohibition on the ability of a covered entity to reduce its outstanding Federal assistance for this purpose.
- "Excessive bonuses" are "applicable bonuses" that are (1) retention bonuses or (2) paid for services rendered in a given year, to the extent the total bonus with respect to such year exceeds $50,000 (with special rules relating to earnings).
    - "Applicable bonuses" are bonuses that are (1) paid in calendar year 2009 or later with respect to services performed in a calendar year in which Federal

assistance was outstanding and (2) in addition to amounts payable at a regular periodic rate for services performed. Excludes commissions, contributions to any qualified retirement plan, welfare and fringe benefits, overtime pay and expense reimbursements.

  - "Retention bonuses" are payments contingent on future service or the completion of a specified project and not based on the performance of the individual.

- Tax is not imposed on:

  - Any portion of a covered bonus which the employee repays prior to the date on which his or her tax return for relevant tax year (i.e., the year in which he or she would otherwise be taxed on the bonus) is due.

  - The following equity awards granted on or after January 1, 2009, provided no portion of the award vests before the third anniversary of the grant date: (1) stock options and stock appreciation rights granted at fair market value and (2) restricted stock awards provided for under § 111(b)(3)(D) of EESA.

  - Any bonus paid after the employer ceases to be a covered entity even if it relates to services performed while the employer was a covered entity.

- Covered entities are required to notify Treasury and employees as soon as practicable after enactment of the amount of excessive bonuses and related tax withholding.

Limitation on Nonqualified Deferred Compensation

- Provides that nonqualified deferred compensation plans of a covered entity (as defined above) must impose a $1 million cap on the aggregate amount that can be deferred by an employee under all such plans with respect to any given year beginning after December 31, 2008 (with special rules relating to earnings).

- Directs Treasury to issue guidance within 60 days allowing employers to amend plans adopted prior to December 31, 2008 to permit participants to terminate their participation in the plan, or cancel or modify outstanding deferral elections with respect to amounts deferred after enactment, to the extent necessary for compliance without such amendments causing violations of § 409A of the Internal Revenue Code.

H.R. 1664

- Deletes the exception for binding contracts from ARRA's prohibition on bonuses payable to senior executive officers and the top 20 most highly paid employees.

- Provides that no TARP recipient may, "while [the government's] capital investment remains outstanding," make a compensation payment (other than a longevity bonus or a restricted stock award) to any employee under any existing arrangement, or enter into a new compensation payment arrangement, if it: (1) provides for compensation that is "unreasonable or excessive" or (2) includes any bonus or other supplemental payment that is not directly based on "performance-based measures."

    - Expressly states that restrictions do not apply to institutions that have done business with TARP recipients.

- Directs Treasury, in consultation with the Chairperson of the Congressional Oversight Panel established under EESA and with the approval of the Federal Financial Institutions Examination Council, to establish, within 30 days of enactment, standards for determining "unreasonable or excessive" compensation and "performance-based measures."

    - "Performance-based measures" established by Treasury must include (1) the stability of the company and its ability to repay TARP funds, (2) the employee's performance, (3) adherence by employees to appropriate risk management requirements and (4) other standards that provide "greater accountability to shareholders and taxpayers."

- Requires that TARP recipients must, within 90 days after enactment and on March 31 each year thereafter, report to Treasury the number of officers, directors and employees who received (or will receive) total compensation in that fiscal year over each of the following thresholds: (i) $500,000, (ii) $1,000,000, (iii) $2,000,000, (iv) $3,000,000 and (v) $5,000,000.

    - "Total compensation" is defined to include all cash payments (including without limitation salary, bonus, retention payments), all transfers of property, stock options, sales of stock, and all contributions by the TARP recipient (or its affiliates) for the individual's benefit.

    - Requires a retrospective annual report for 2008, and both a prospective and a retrospective annual report for each subsequent calendar year until the institution has repaid its obligations under TARP.

  - The report need not identify individuals by name, but must distinguish amounts the TARP recipient considers to be a bonus and the reason for such distinction.

  - Treasury will make these reports available on the internet.

- New restrictions also apply to Fannie Mae, Freddie Mac and any Federal home loan bank while any capital investment remains outstanding under the amendments made by section 1117 of the Housing and Economic Recovery Act of 2008.

H.R. 1575 (the "End Government Reimbursement of Excessive Executive Disbursements (End GREED) Act")

- Authorizes Attorney General, after consultation with Treasury, to review (1) any employment contract made by a "recipient entity" and (2) any payment made on or after September 1, 2008 by a recipient entity to an employee.

  - "Employment contract" includes an employment contract that provides for the payment of compensation (including performance or incentive compensation, a bonus of any kind, or any other financial return designed to replace or enhance incentive, stock or other compensation).

- "Recipient entity" is defined as any entity (including any subsidiaries) that received, on or after September 1, 2008, a line of credit or loan, a payment in exchange for the entity's stock (or stock of such subsidiaries), or any combination of credit, loans or payments, that exceeds $10 billion in the aggregate.

- Provides that Attorney General may commence a civil action in US district court to:

  - Avoid payment by a recipient entity to an employee (including under an employment contract) if the entity (1) "received less than a reasonably equivalent value in exchange for such payment" and (2) was either (a) insolvent on the date of the payment (not taking into account Government assistance received on or after September 1, 2008) or (b) engaged, or about to engage, in business or a transaction "for which property remaining in the recipient entity was an unreasonably small capital."

    - Applies to all payments made on or after September 1, 2008.

    - Attorney General can avoid any transfer of a recipient entity's property, or any obligation incurred by the entity, to an employee that is avoidable under law by a creditor holding an unsecured claim against the entity.

- Limit the amount of compensation paid or payable on or after the date of enactment by a recipient entity under an employment contract if such compensation is greater than 10x the mean amount of compensation paid or payable to non-management employees of the entity for any purpose during the calendar year in which such compensation was paid or payable.

- Authorizes Attorney General to issue subpoenas requiring attendance and testimony of witnesses and production of documents relating to matters relevant to implementation of the legislation, which subpoenas are enforceable by court order.

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Please contact A. Richard Susko, Arthur H. Kohn or Mary E. Alcock, any of the lawyers listed in the Corporate Governance or Employee Benefits section of our website (www.cgsh.com) or any of your other regular contacts at the firm for further information about the matters discussed above.

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H. R. 1

One Hundred Eleventh Congress of the United States of America

AT THE FIRST SESSION

Begun and held at the City of Washington on Tuesday, the sixth day of January, two thousand and nine

An Act

Making supplemental appropriations for job preservation and creation, infrastructure investment, energy efficiency and science, assistance to the unemployed, and State and local fiscal stabilization, for the fiscal year ending September 30, 2009, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "American Recovery and Reinvestment Act of 2009".

SEC. 2. TABLE OF CONTENTS.

The table of contents for this Act is as follows:

SEC. 3. PURPOSES AND PRINCIPLES.

(a) STATEMENT OF PURPOSES.—The purposes of this Act include the following:

(2) The national broadband plan required by this section shall seek to ensure that all people of the United States have access to broadband capability and shall establish benchmarks for meeting that goal. The plan shall also include—

(A) an analysis of the most effective and efficient mechanisms for ensuring broadband access by all people of the United States;

(B) a detailed strategy for achieving affordability of such service and maximum utilization of broadband infrastructure and service by the public;

(C) an evaluation of the status of deployment of broadband service, including progress of projects supported by the grants made pursuant to this section; and

(D) a plan for use of broadband infrastructure and services in advancing consumer welfare, civic participation, public safety and homeland security, community development, health care delivery, energy independence and efficiency, education, worker training, private sector investment, entrepreneurial activity, job creation and economic growth, and other national purposes.

(3) In developing the plan, the Commission shall have access to data provided to other Government agencies under the Broadband Data Improvement Act (47 U.S.C. 1301 note).

(l) The Assistant Secretary shall develop and maintain a comprehensive nationwide inventory map of existing broadband service capability and availability in the United States that depicts the geographic extent to which broadband service capability is deployed and available from a commercial provider or public provider throughout each State. Not later than 2 years after the date of the enactment of this Act, the Assistant Secretary shall make the broadband inventory map developed and maintained pursuant to this section accessible by the public on a World Wide Web site of the National Telecommunications and Information Administration in a form that is interactive and searchable.

(m) The Assistant Secretary shall have the authority to prescribe such rules as are necessary to carry out the purposes of this section.

TITLE VII—LIMITS ON EXECUTIVE COMPENSATION

SEC. 7000. TABLE OF CONTENTS.

The table of contents of this title is as follows:

SEC. 7001. EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.

Section 111 of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5221) is amended to read as follows:

"SEC. 111. EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.

"(a) DEFINITIONS.—For purposes of this section, the following definitions shall apply:

"(1) SENIOR EXECUTIVE OFFICER.—The term 'senior executive officer' means an individual who is 1 of the top 5 most highly paid executives of a public company, whose compensation is required to be disclosed pursuant to the Securities Exchange Act of 1934, and any regulations issued thereunder, and nonpublic company counterparts.

"(2) GOLDEN PARACHUTE PAYMENT.—The term 'golden parachute payment' means any payment to a senior executive officer for departure from a company for any reason, except for payments for services performed or benefits accrued.

"(3) TARP RECIPIENT.—The term 'TARP recipient' means any entity that has received or will receive financial assistance under the financial assistance provided under the TARP.

"(4) COMMISSION.—The term 'Commission' means the Securities and Exchange Commission.

"(5) PERIOD IN WHICH OBLIGATION IS OUTSTANDING; RULE OF CONSTRUCTION.—For purposes of this section, the period in which any obligation arising from financial assistance provided under the TARP remains outstanding does not include any period during which the Federal Government only holds warrants to purchase common stock of the TARP recipient.

"(b) EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.—

"(1) ESTABLISHMENT OF STANDARDS.—During the period in which any obligation arising from financial assistance provided under the TARP remains outstanding, each TARP recipient shall be subject to—

"(A) the standards established by the Secretary under this section; and

"(B) the provisions of section 162(m)(5) of the Internal Revenue Code of 1986, as applicable.

"(2) STANDARDS REQUIRED.—The Secretary shall require each TARP recipient to meet appropriate standards for executive compensation and corporate governance.

"(3) SPECIFIC REQUIREMENTS.—The standards established under paragraph (2) shall include the following:

"(A) Limits on compensation that exclude incentives for senior executive officers of the TARP recipient to take unnecessary and excessive risks that threaten the value of such recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding.

"(B) A provision for the recovery by such TARP recipient of any bonus, retention award, or incentive compensation paid to a senior executive officer and any of the next 20 most highly-compensated employees of the TARP recipient based on statements of earnings, revenues, gains, or other criteria that are later found to be materially inaccurate.

"(C) A prohibition on such TARP recipient making any golden parachute payment to a senior executive officer or any of the next 5 most highly-compensated employees of the TARP recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding.

"(D)(i) A prohibition on such TARP recipient paying or accruing any bonus, retention award, or incentive compensation during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding, except that any prohibition developed under this paragraph shall not apply to the payment of long-term restricted stock by such TARP recipient, provided that such long-term restricted stock—

"(I) does not fully vest during the period in which any obligation arising from financial assistance provided to that TARP recipient remains outstanding;

"(II) has a value in an amount that is not greater than ⅓ of the total amount of annual compensation of the employee receiving the stock; and

"(III) is subject to such other terms and conditions as the Secretary may determine is in the public interest.

"(ii) The prohibition required under clause (i) shall apply as follows:

"(I) For any financial institution that received financial assistance provided under the TARP equal to less than $25,000,000, the prohibition shall apply only to the most highly compensated employee of the financial institution.

"(II) For any financial institution that received financial assistance provided under the TARP equal to at least $25,000,000, but less than $250,000,000, the prohibition shall apply to at least the 5 most highly-compensated employees of the financial institution, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

"(III) For any financial institution that received financial assistance provided under the TARP equal to at least$250,000,000, but less than $500,000,000, the prohibition shall apply to the senior executive officers and at least the 10 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

"(IV) For any financial institution that received financial assistance provided under the TARP equal to $500,000,000 or more, the prohibition shall apply to the senior executive officers and at least the 20 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

"(iii) The prohibition required under clause (i) shall not be construed to prohibit any bonus payment required to be paid pursuant to a written employment contract executed on or before February 11, 2009, as such valid employment contracts are determined by the Secretary or the designee of the Secretary.

"(E) A prohibition on any compensation plan that would encourage manipulation of the reported earnings of such

TARP recipient to enhance the compensation of any of its employees.

"(F) A requirement for the establishment of a Board Compensation Committee that meets the requirements of subsection (c).

"(4) CERTIFICATION OF COMPLIANCE.—The chief executive officer and chief financial officer (or the equivalents thereof) of each TARP recipient shall provide a written certification of compliance by the TARP recipient with the requirements of this section—

"(A) in the case of a TARP recipient, the securities of which are publicly traded, to the Securities and Exchange Commission, together with annual filings required under the securities laws; and

"(B) in the case of a TARP recipient that is not a publicly traded company, to the Secretary.

"(c) BOARD COMPENSATION COMMITTEE.—

"(1) ESTABLISHMENT OF BOARD REQUIRED.—Each TARP recipient shall establish a Board Compensation Committee, comprised entirely of independent directors, for the purpose of reviewing employee compensation plans.

"(2) MEETINGS.—The Board Compensation Committee of each TARP recipient shall meet at least semiannually to discuss and evaluate employee compensation plans in light of an assessment of any risk posed to the TARP recipient from such plans.

"(3) COMPLIANCE BY NON-SEC REGISTRANTS.—In the case of any TARP recipient, the common or preferred stock of which is not registered pursuant to the Securities Exchange Act of 1934, and that has received $25,000,000 or less of TARP assistance, the duties of the Board Compensation Committee under this subsection shall be carried out by the board of directors of such TARP recipient.

"(d) LIMITATION ON LUXURY EXPENDITURES.—The board of directors of any TARP recipient shall have in place a companywide policy regarding excessive or luxury expenditures, as identified by the Secretary, which may include excessive expenditures on—

"(1) entertainment or events;

"(2) office and facility renovations;

"(3) aviation or other transportation services; or

"(4) other activities or events that are not reasonable expenditures for staff development, reasonable performance incentives, or other similar measures conducted in the normal course of the business operations of the TARP recipient.

"(e) SHAREHOLDER APPROVAL OF EXECUTIVE COMPENSATION.—

"(1) ANNUAL SHAREHOLDER APPROVAL OF EXECUTIVE COMPENSATION.—Any proxy or consent or authorization for an annual or other meeting of the shareholders of any TARP recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding shall permit a separate shareholder vote to approve the compensation of executives, as disclosed pursuant to the compensation disclosure rules of the Commission (which disclosure shall include the compensation discussion and analysis, the compensation tables, and any related material).

"(2) NONBINDING VOTE.—A shareholder vote described in paragraph (1) shall not be binding on the board of directors of a TARP recipient, and may not be construed as overruling a decision by such board, nor to create or imply any additional fiduciary duty by such board, nor shall such vote be construed to restrict or limit the ability of shareholders to make proposals for inclusion in proxy materials related to executive compensation.

"(3) DEADLINE FOR RULEMAKING.—Not later than 1 year after the date of enactment of the American Recovery and Reinvestment Act of 2009, the Commission shall issue any final rules and regulations required by this subsection.

"(f) REVIEW OF PRIOR PAYMENTS TO EXECUTIVES.—

"(1) IN GENERAL.—The Secretary shall review bonuses, retention awards, and other compensation paid to the senior executive officers and the next 20 most highly-compensated employees of each entity receiving TARP assistance before the date of enactment of the American Recovery and Reinvestment Act of 2009, to determine whether any such payments were inconsistent with the purposes of this section or the TARP or were otherwise contrary to the public interest.

"(2) NEGOTIATIONS FOR REIMBURSEMENT.—If the Secretary makes a determination described in paragraph (1), the Secretary shall seek to negotiate with the TARP recipient and the subject employee for appropriate reimbursements to the Federal Government with respect to compensation or bonuses.

"(g) NO IMPEDIMENT TO WITHDRAWAL BY TARP RECIPIENTS.—Subject to consultation with the appropriate Federal banking agency (as that term is defined in section 3 of the Federal Deposit Insurance Act), if any, the Secretary shall permit a TARP recipient to repay any assistance previously provided under the TARP to such financial institution, without regard to whether the financial institution has replaced such funds from any other source or to any waiting period, and when such assistance is repaid, the Secretary shall liquidate warrants associated with such assistance at the current market price.

"(h) REGULATIONS.—The Secretary shall promulgate regulations to implement this section.".

SEC. 7002. APPLICABILITY WITH RESPECT TO LOAN MODIFICATIONS.

Section 109(a) of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5219(a)) is amended—

(1) by striking "To the extent" and inserting the following: "(1) IN GENERAL.—To the extent"; and

(2) by adding at the end the following:

"(2) WAIVER OF CERTAIN PROVISIONS IN CONNECTION WITH LOAN MODIFICATIONS.—The Secretary shall not be required to apply executive compensation restrictions under section 111, or to receive warrants or debt instruments under section 113, solely in connection with any loan modification under this section.".

Speaker of the House of Representatives.

Vice President of the United States and President of the Senate.

II

Calendar No. 36

111TH CONGRESS
1ST SESSION

H. R. 1586

IN THE SENATE OF THE UNITED STATES

MARCH 19, 2009

Received and read the first time

MARCH 23, 2009

Read the second time and placed on the calendar

AN ACT

To impose an additional tax on bonuses received from certain TARP recipients.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. BONUSES RECEIVED FROM CERTAIN TARP RECIPIENTS.

(a) IN GENERAL.—In the case of an employee or former employee of a covered TARP recipient, the tax imposed by chapter 1 of the Internal Revenue Code of 1986 for any taxable year shall not be less than the sum of—

(1) the tax that would be determined under such chapter if the taxable income of the taxpayer

for such taxable year were reduced (but not below zero) by the TARP bonus received by the taxpayer during such taxable year, plus

(2) 90 percent of the TARP bonus received by the taxpayer during such taxable year.

(b) TARP BONUS.—For purposes of this section—

(1) IN GENERAL.—The term ''TARP bonus'' means, with respect to any individual for any taxable year, the lesser of—

(A) the aggregate disqualified bonus payments received from covered TARP recipients during such taxable year, or

(B) the excess of—

(i) the adjusted gross income of the taxpayer for such taxable year, over

(ii) $250,000 ($125,000 in the case of a married individual filing a separate return).

(2) DISQUALIFIED BONUS PAYMENT.—

(A) IN GENERAL.—The term ''disqualified bonus payment'' means any retention payment, incentive payment, or other bonus which is in addition to any amount payable to such individual for service performed by such individual at a regular hourly, daily, weekly, monthly, or similar periodic rate.

(B) EXCEPTIONS.—Such term shall not include commissions, welfare or fringe benefits, or expense reimbursements.

(C) WAIVER OR RETURN OF PAYMENTS.—Such term shall not include any amount if the employee irrevocably waives the employee's entitlement to such payment, or the employee returns such payment to the employer, before the close of the taxable year in which such payment is due. The preceding sentence shall not apply if the employee receives any benefit from the employer in connection with the waiver or return of such payment.

(3) REIMBURSEMENT OF TAX TREATED AS TARP BONUS.—Any reimbursement by a covered TARP recipient of the tax imposed under subsection (a) shall be treated as a disqualified bonus payment to the taxpayer liable for such tax.

(c) COVERED TARP RECIPIENT.—For purposes of this section—

(1) IN GENERAL.—The term ''covered TARP recipient'' means—

(A) any person who receives after December 31, 2007, capital infusions under the Emergency Economic Stabilization Act of 2008 which, in the aggregate, exceed $5,000,000,000,

(B) the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation,

(C) any person who is a member of the same affiliated group (as defined in section 1504 of the Internal Revenue Code of 1986, determined without regard to paragraphs (2) and (3) of subsection (b)) as a person described in subparagraph (A) or (B), and

(D) any partnership if more than 50 percent of the capital or profits interests of such partnership are owned directly or indirectly by one or more persons described in subparagraph (A), (B), or (C).

(2) EXCEPTION FOR TARP RECIPIENTS WHO REPAY ASSISTANCE.—A person shall be treated as described in paragraph (1)(A) for any period only if—

(A) the excess of the aggregate amount of capital infusions described in paragraph (1)(A) with respect to such person over the amounts repaid by such person to the Federal Government with respect to such capital infusions, exceeds

(B) $5,000,000,000.

(d) OTHER DEFINITIONS.—Terms used in this section which are also used in the Internal Revenue Code of 1986 shall have the same meaning when used in this section as when used in such Code.

(e) COORDINATION WITH INTERNAL REVENUE CODE OF 1986.—Any increase in the tax imposed under chapter 1 of the Internal Revenue Code of 1986 by reason of subsection (a) shall not be treated as a tax imposed by such chapter for purposes of determining the amount of any credit under such chapter or for purposes of section 55 of such Code.

(f) REGULATIONS.—The Secretary of the Treasury, or the Secretary's delegate, shall prescribe such regulations or other guidance as may be necessary or appropriate to carry out the purposes of this section.

(g) EFFECTIVE DATE.—This section shall apply to disqualified bonus payments received after December 31, 2008, in taxable years ending after such date.

Passed the House of Representatives March 19, 2009.

Attest: LORRAINE C. MILLER,

Clerk.

Calendar No. 36

111TH CONGRESS
1ST SESSION

H. R. 1586

AN ACT

To impose an additional tax on bonuses received from certain TARP recipients.

MARCH 23, 2009

Read the second time and placed on the calendar

II

Calendar No. 37

111TH CONGRESS
1ST SESSION

S. 651

To amend the Internal Revenue Code of 1986 to impose an excise tax on excessive bonuses paid by, and received from, companies receiving Federal emergency economic assistance, to limit the amount of nonqualified deferred compensation that employees of such companies may defer from taxation, and for other purposes.

IN THE SENATE OF THE UNITED STATES

MARCH 19, 2009

Mr. BAUCUS (for himself, Mr. GRASSLEY, Mr. WYDEN, Ms. SNOWE, Mrs. LINCOLN, Mr. KERRY, Ms. STABENOW, Mr. SCHUMER, Mr. MENENDEZ, Mr. NELSON of Florida, Mr. BINGAMAN, and Ms. CANTWELL) introduced the following bill; which was read the first time

MARCH 23, 2009

Read the second time and placed on the calendar

A BILL

To amend the Internal Revenue Code of 1986 to impose an excise tax on excessive bonuses paid by, and received from, companies receiving Federal emergency economic assistance, to limit the amount of nonqualified deferred compensation that employees of such companies may defer from taxation, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the ‘‘Compensation Fairness Act of 2009’’.

SEC. 2. EXCISE TAXES ON EXCESSIVE BONUSES PAID BY RECIPIENTS OF FEDERAL EMERGENCY ECONOMIC ASSISTANCE.

(a) IMPOSITION OF TAX.—Chapter 46 of the Internal Revenue Code of 1986 (relating to excise tax on golden parachute payments) is amended by adding at the end the following new section:

‘‘SEC. 4999A. EXCESSIVE BONUSES PAID BY RECIPIENTS OF FEDERAL EMERGENCY ECONOMIC ASSISTANCE.

‘‘(a) IMPOSITION OF TAX.—There is hereby imposed—

‘‘(1) on each Federal emergency economic assistance recipient which pays an excessive bonus, a tax equal to 35 percent of the amount of such bonus, and

‘‘(2) on each covered individual who receives an excessive bonus from such a recipient, a tax equal to 35 percent of the amount of such bonus.

‘‘(b) EXCESSIVE BONUS.—For purposes of this section—

‘‘(1) IN GENERAL.—The term ‘excessive bonus’ means, with respect to any calendar year—

"(A) any applicable bonus payment paid to a covered individual during such calendar year which is a retention bonus, or

"(B) in the case of applicable bonus payments not described in subparagraph (A), an amount equal to the sum of—

"(i) the portion of such applicable bonus payments paid to a covered individual during such calendar year which is attributable to services performed by such individual during such calendar year, but only to the extent such payments exceed $50,000, plus

"(ii) the portion of applicable bonus payments paid to a covered individual during such calendar year which is attributable to services performed by such individual during any preceding calendar year, but only to the extent such payments (when added to such payments paid during all prior calendar years with respect to services performed during such preceding calendar year) exceed $50,000.

"(2) APPLICABLE BONUS PAYMENTS.—

"(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'applicable bonus payment' means any bonus payment by a Federal emergency economic assistance recipient—

"(i) which is paid after December 31, 2008, and

"(ii) which is payable by reason of services performed by such individual in an applicable calendar year of the Federal emergency economic assistance recipient.

"(B) PAYMENTS AFTER ASSISTANCE PERIOD.—A bonus payment shall not be treated as an applicable bonus payment if it is made after the end date applicable under clause (i)(II) or (ii)(II) of subparagraph (C) (without regard to whether the payment is attributable to services performed before such end date).

"(C) APPLICABLE CALENDAR YEAR.—The term 'applicable calendar year' means, with respect to any Federal emergency economic assistance recipient, any calendar year which includes any portion of the period which—

"(i) in the case of a recipient described in subsection (c)(1)—

"(I) begins on the first date on which the outstanding aggregate assistance received under all programs described in subsection (c)(1)(A) exceeds $100,000,000, and

"(II) ends on the first date on which such outstanding aggregate amount does not exceed $100,000,000, and

"(ii) in the case of a recipient described in subsection (c)(2)—

"(I) begins on the first date on which assistance was received under a program described in subsection (c)(1)(A), and

"(II) ends on the first date on which there is no outstanding assistance provided to such recipient under any such program.

In the case of a person described in subsection (c)(3) with respect to a recipient described in subsection (c)(1) or (2), this subparagraph shall be applied by reference to the same period as is used for such recipient.

"(D) WAIVER OF RESTRICTION ON REPAYMENT OR REDEMPTION.—Any restriction or prohibition under any program described in subsection (c)(1)(A) (or any agreement entered into under such program) on a Federal emergency economic assistance recipient with respect to the repayment of any assistance provided under such program or the redemption of any equity interest shall not apply if such restriction or prohibition would prevent the recipient from reducing its outstanding assistance for purposes of subparagraph (C).

"(3) BONUS PAYMENT.—

"(A) IN GENERAL.—The term 'bonus payment' means any payment which—

"(i) is a payment to a covered individual by a Federal emergency economic assistance recipient for services rendered, and

"(ii) is in addition to any amount payable to such individual for services performed by such individual at a regular hourly, daily, weekly, monthly, or similar periodic rate.

Such term does not include payments to an employee as commissions, contributions to any qualified retirement plan (as defined in section 4974(c)), welfare and fringe benefits, overtime pay, or expense reimbursements.

"(B) EXCEPTION FOR CERTAIN EQUITY PAYMENTS.—

"(i) IN GENERAL.—In the case of a payment other than a retention bonus, such payment shall not be treated as a bonus payment if the payment consists of the granting on or after January 1, 2009, of an equity interest described in clause (ii) but only if no portion of such interest vests before the date which is 3 years after the date on which such interest is granted.

"(ii) EQUITY INTERESTS.—An equity interest is described in this clause if it is—

"(I) a stock option which is granted at its fair market value on the date of the grant,

"(II) a stock appreciation right which is granted at its fair market value on the date of the grant, or

"(III) restricted stock described in section 111(b)(3)(D)(i) of the Emergency Economic Stabilization Act of 2008 (as in effect on the date of the enactment of this section).

"(iii) SECRETARIAL AUTHORITY.—The Secretary may by regulation provide for the application of this subparagraph in the case of a person other than a corporation.

"(4) RETENTION BONUS.—The term 'retention bonus' means any bonus payment to an individual which—

"(A) is contingent on the completion of a period of future service with the Federal emergency economic assistance recipient, the completion of a specific project or other activity for the Federal emergency economic assistance recipient, or such other circumstances as the Secretary may prescribe, and

"(B) is not based on the performance of the individual (other than a requirement that the employee not be separated from employment for cause).

A bonus payment shall not be treated as based on performance for purposes of subparagraph (B) solely because the amount of the payment is determined by reference to a previous bonus payment which was based on performance.

"(c) FEDERAL EMERGENCY ECONOMIC ASSISTANCE RECIPIENT.—For purposes of this subsection, the term 'Federal emergency economic assistance recipient' means—

"(1) any person (other than a bank to which section 585 applies) if at any time after December 31, 2007—

"(A) the Federal Government acquires—

"(i) an equity interest in such person pursuant to a program authorized by the Emergency Economic Stabilization Act of 2008 or the third undesignated paragraph of section 13 of the Federal Reserve Act (12 U.S.C. 343), or

"(ii) any warrant (or other right) to acquire any equity interest with respect to such person pursuant to any such program, and

"(B) the outstanding aggregate amount of the assistance provided to such person under such programs exceeds $100,000,000,

"(2) the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation, and

"(3) any person which is a member of the same affiliated group (as defined in section 1504, determined without regard to subsection (b) thereof) as a person described in paragraph (1) or (2).

"(d) COVERED INDIVIDUAL.—For purposes of this section, the term 'covered individual' means, with respect to any Federal emergency economic assistance recipient, any director or officer or other employee of such recipient.

"(e) ADMINISTRATIVE PROVISIONS; SPECIAL RULES.—For purposes of this section—

"(1) ADMINISTRATIVE PROVISIONS.—

"(A) IN GENERAL.—For purposes of subtitle F, the tax imposed by this section with respect to an excessive bonus shall be treated as a tax imposed by subtitle A for the taxable year of the Federal emergency economic assistance recipient or covered individual with or within which ends the calendar year in which payment of the excessive bonus is made.

"(B) WAGE WITHHOLDING.—If an excessive bonus is treated as wages for purposes of section 3402, the amount otherwise required to be deducted and withheld under such section shall be increased by an amount equal to 35 percent of such bonus.

"(C) SPECIAL RULES FOR PAYMENTS TO NONRESIDENT ALIEN INDIVIDUALS.—In the case of a payment of an excessive bonus to a covered individual who is a nonresident alien individual—

"(i) WITHHOLDING.—If section 1441 applies with respect to such payment, the amount otherwise required to be deducted and withheld under such section shall be increased by an amount equal to 35 percent of such bonus.

"(ii) LIABILITY WHERE NO WITHHOLDING.—If section 1441 does not apply to such payment, the person described in subsection (c)(1) or (2) with respect to the excessive bonus (and all persons described in subsection (c)(3) with respect to such person) shall be jointly and severally liable for payment of the tax imposed by subsection (a)(2) with respect to the excessive bonus.

"(2) SPECIAL RULES FOR EARNINGS.—

"(A) INCLUSION OF FUTURE EARNINGS ON EXCESSIVE BONUSES.—Any income (whether actual or notional) for any calendar year which is properly allocable to the portion of any applicable bonus payment which is treated as an excessive bonus (determined after application of subparagraph (B)) shall be treated as an excessive bonus for the calendar year in which paid.

"(B) FUTURE EARNINGS ON PAYMENT NOT TREATED AS EXCESSIVE BONUS.—

"(i) IN GENERAL.—Any income (whether actual or notional) for any calendar year which is properly allocable to the portion of any applicable bonus payment which is not treated as an excessive bonus shall be taken into account as an excessive bonus in the calendar year in which paid to the extent that the sum of—

"(I) the amount of such income in excess of the amount which would have been earned if the return on such portion were a market rate of return, plus

"(II) an amount equal to such portion, plus

"(III) such excess income for any preceding calendar year,

exceeds $50,000.

"(ii) MARKET RATE OF RETURN.—The Secretary shall prescribe by regulation rules governing the calculation of a market rate of return. Such rules shall allow in appropriate cases the treatment of income as based on a market rate of return if the income of the plan is determined by reference to the rate of return on a predetermined investment, including stock or other ownership interests (whether or not publicly traded) in the employer maintaining the plan.

"(3) INDIVIDUAL NOT TAXED IF BONUS REPAID.—If a covered individual repays all or any portion of an applicable bonus payment to the Federal emergency economic assistance recipient before the due date (without regard to extensions) for the individual's return of tax imposed by chapter for the taxable year for which tax under this section would (without regard to this paragraph) have been imposed, then, solely for purposes of applying this title to the covered individual, the portion repaid shall be treated as if it had not been paid to the covered individual.

"(4) NOTICE REQUIREMENTS.—The Secretary shall require each Federal emergency economic assistance recipient to notify, as soon as practicable after the date of the enactment of this subsection and at such other times as the Secretary determines appropriate, the Secretary and each covered individual of the amount of excessive bonuses to which this section applied and the amount of tax deducted and withheld on such bonuses.

"(5) SECRETARIAL AUTHORITY.—The Secretary may prescribe such regulations, rules, and guidance as may be necessary to carry out the provisions of this section, including regulations, rules, and guidance necessary to prevent—

"(A) the recharacterization of a bonus payment as a payment which is not a bonus payment in order to avoid the purposes of this section, or

"(B) the avoidance of the purposes of this section through the use of partnerships or other pass through entities.".

(b) CONFORMING AMENDMENTS.—

(1) The heading and table of sections for chapter 46 of such Code are amended to read as follows:

"CHAPTER 46-TAXES ON CERTAIN EXCESSIVE REMUNERATION

"Sec. 4999. Golden parachute payments.
"Sec. 4999A. Excessive bonuses paid by recipients of Federal emergency economic assistance.".

(2) The item relating to chapter 46 in the table of chapters for subtitle D of such Code is amended to read as follows:

"Chapter 46. Taxes on excessive remuneration.".

(c) EFFECTIVE DATE.—The amendments made by this subsection shall apply to payments of excessive bonuses after December 31, 2008, in taxable years ending after such date.

SEC. 3. LIMITATION ON ANNUAL AMOUNTS WHICH MAY BE DEFERRED UNDER NONQUALIFIED DEFERRED COMPENSATION ARRANGEMENTS OF RECIPIENTS OF FEDERAL EMERGENCY ECONOMIC ASSISTANCE.

(a) IN GENERAL.—Section 409A(a) of the Internal Revenue Code of 1986 (relating to inclusion of gross income under nonqualified deferred compensation plans) is amended—

(1) by striking "and (4)" in subclause (I) of paragraph (1)(A)(i) and inserting "(4), and (5)", and

(2) by adding at the end the following new paragraph:

"(5) ANNUAL LIMITATION ON AGGREGATE DEFERRED AMOUNTS.—

"(A) LIMITATION.—In the case of any Federal emergency economic assistance recipient maintaining a nonqualified deferred compensation plan, the requirements of this paragraph are met if the plan provides that the aggregate amount of compensation which is deferred for any applicable taxable year beginning after December 31, 2008, with respect to a participant under the plan may not exceed $1,000,000. For purposes of this paragraph, only amounts deferred after the date of the enactment of this paragraph shall be taken into account.

"(B) SPECIAL RULES RELATING TO EARNINGS.—

"(i) INCLUSION OF FUTURE EARNINGS.—If an amount is includible under paragraph (1) in the gross income of a participant for any taxable year by reason of any failure to meet the requirements of this paragraph, any income (whether actual or notional) for any subsequent taxable year shall be included in gross income under paragraph (1)(A) in such subsequent taxable year to the extent such income—

"(I) is attributable to compensation (or income attributable to such compensation) required to be included in gross income by reason of such failure (including by reason of this subparagraph), and

"(II) is not subject to a substantial risk of forfeiture and has not been previously included in gross income.

"(ii) EARNINGS COUNTED AGAINST CAP ONLY IF IN EXCESS OF MARKET RATE.—Income (whether actual or notional) which is properly allocable to any participant for any taxable year shall be taken into account in determining whether the requirement of subparagraph (A) is met with respect to the taxable year only to the extent of the excess (if any) of—

"(I) the amount of such income, over

"(II) the amount of such income which would have been earned on the amount to which it is attributable if the return on such amount were a market rate of return.

"(iii) MARKET RATE OF RETURN.—The Secretary shall prescribe by regulation rules governing the calculation of a market rate of return. Such rules shall allow in appropriate cases the treatment of income as based on a market rate of return if the income of the plan is determined by reference to the rate of return on a predetermined investment, including stock or other ownership interests (whether or not publicly traded) in the employer maintaining the plan.

"(C) AGGREGATION RULE.—For purposes of this paragraph, all nonqualified deferred compensation plans maintained by all employers treated as a single employer under subsection (d)(6) shall be treated as 1 plan.

"(D) DEFINITIONS.—For purposes of this paragraph—

"(i) IN GENERAL.—Any term which is used in this paragraph which is also used in section 4999A shall have the same meaning as when used in such section.

"(ii) APPLICABLE TAXABLE YEAR.—The term 'applicable taxable year' means any taxable year which includes the portion of any applicable calendar year (as defined in section 4999A(b)(2)(C)).".

(b) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 2008, except that the amendments shall only apply to amounts deferred after the date of the enactment of this Act (and to earnings on such amounts).

(2) GUIDANCE RELATING TO CERTAIN EXISTING ARRANGEMENTS.—Not later than 60 days after the date of the enactment of this Act, the Secretary of the Treasury shall issue guidance providing a limited period during which a nonqualified deferred com-

pensation plan adopted before December 31, 2008, may, without violating the requirements of section 409A(a) of such Code, be amended—

(A) to provide that a participant may, no later than December 31, 2009—

(i) terminate participation in the plan, or

(ii) cancel or modify an outstanding deferral election with regard to all or a portion of amounts deferred after the date of the enactment of this Act, to the extent necessary for the plan to meet the requirements of section 409A(a)(5) of such Code (as added by the amendments made by this section),

but only if amounts subject to the termination, cancellation, or modification are, to the extent not previously included in gross income, includible in income of the participant when no longer subject to substantial risk of forfeiture, and

(B) to conform to the requirements of section 409A(a)(5) of such Code (as added by the amendments made by this section) with regard to amounts deferred after the date of the enactment of this Act.

Calendar No. 37

111TH CONGRESS
1ST SESSION

S. 651

A BILL

To amend the Internal Revenue Code of 1986 to impose an excise tax on excessive bonuses paid by, and received from, companies receiving Federal emergency economic assistance, to limit the amount of nonqualified deferred compensation that employees of such companies may defer from taxation, and for other purposes.

MARCH 23, 2009

Read the second time and placed on the calendar

Following is the text of ARRA, as revised by H.R. 1664 (as passed by the House Committee on Financial Services on March 25, 2009). Changes to ARRA as proposed by H.R. 1664 appear in <u>underlined text</u>.

TITLE VII--LIMITS ON EXECUTIVE COMPENSATION

SEC. 7000. TABLE OF CONTENTS.

The table of contents of this title is as follows:

TITLE VII--LIMITS ON EXECUTIVE COMPENSATION

SEC. 7001. EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.

Section 111 of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5221) is amended to read as follows:

`SEC. 111. EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.

`(a) Definitions- For purposes of this section, the following definitions shall apply:

`(1) SENIOR EXECUTIVE OFFICER- The term `senior executive officer' means an individual who is 1 of the top 5 most highly paid executives of a public company, whose compensation is required to be disclosed pursuant to the Securities Exchange Act of 1934, and any regulations issued thereunder, and non-public company counterparts.

`(2) GOLDEN PARACHUTE PAYMENT- The term `golden parachute payment' means any payment to a senior executive officer for departure from a company for any reason, except for payments for services performed or benefits accrued.

`(3) TARP RECIPIENT- The term `TARP recipient' means any entity that has received or will receive financial assistance under the financial assistance provided under the TARP.

`(4) COMMISSION- The term `Commission' means the Securities and Exchange Commission.

`(5) PERIOD IN WHICH OBLIGATION IS OUTSTANDING; RULE OF CONSTRUCTION- For purposes of this section, the period in which any obligation arising from financial assistance provided under the TARP remains outstanding does not include any period during which the Federal Government only holds warrants to purchase common stock of the TARP recipient.

`(b) Executive Compensation and Corporate Governance-

`(1) ESTABLISHMENT OF STANDARDS- During the period in which any obligation arising from financial assistance provided under the TARP remains outstanding, each TARP recipient shall be subject to--

`(A) the standards established by the Secretary under this section; and

`(B) the provisions of section 162(m)(5) of the Internal Revenue Code of 1986, as applicable.

`(2) STANDARDS REQUIRED- The Secretary shall require each TARP recipient to meet appropriate standards for executive compensation and corporate governance.

`(3) SPECIFIC REQUIREMENTS- The standards established under paragraph (2) shall include the following:

`(A) Limits on compensation that exclude incentives for senior executive officers of the TARP recipient to take unnecessary and excessive risks that threaten the value of such recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding.

`(B) A provision for the recovery by such TARP recipient of any bonus, retention award, or incentive compensation paid to a senior executive officer and any of the next 20 most highly-compensated employees of the TARP recipient based on statements of earnings, revenues, gains, or other criteria that are later found to be materially inaccurate.

`(C) A prohibition on such TARP recipient making any golden parachute payment to a senior executive officer or any of the next 5 most highly-compensated employees of the TARP recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding.

`(D)(i) A prohibition on such TARP recipient paying or accruing any bonus, retention award, or incentive compensation during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding, except that any prohibition developed under this paragraph shall not apply to the payment of long-term restricted stock by such TARP recipient, provided that such long-term restricted stock--

`(I) does not fully vest during the period in which any obligation arising from financial assistance provided to that TARP recipient remains outstanding;

`(II) has a value in an amount that is not greater than 1/3 of the total amount of annual compensation of the employee receiving the stock; and

`(III) is subject to such other terms and conditions as the Secretary may determine is in the public interest.

`(ii) The prohibition required under clause (i) shall apply as follows:

`(I) For any financial institution that received financial assistance provided under the TARP equal to less than $25,000,000, the prohibition shall apply only to the most highly compensated employee of the financial institution.

`(II) For any financial institution that received financial assistance provided under the TARP equal to at least

$25,000,000, but less than $250,000,000, the prohibition shall apply to at least the 5 most highly-compensated employees of the financial institution, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

`(III) For any financial institution that received financial assistance provided under the TARP equal to at least$250,000,000, but less than $500,000,000, the prohibition shall apply to the senior executive officers and at least the 10 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

`(IV) For any financial institution that received financial assistance provided under the TARP equal to $500,000,000 or more, the prohibition shall apply to the senior executive officers and at least the 20 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

`(iii) The prohibition required under clause (i) shall not be construed to prohibit any bonus payment required to be paid pursuant to a written employment contract executed on or before February 11, 2009, as such valid employment contracts are determined by the Secretary or the designee of the Secretary, <u>except that an entity subject to subsection (e) may not, while a capital investment described in that subsection remains outstanding, pay a bonus or other supplemental payment that is otherwise prohibited by clause (i) without regard to when the arrangement to pay such a bonus was entered into.</u>

`(E) A prohibition on any compensation plan that would encourage manipulation of the reported earnings of such TARP recipient to enhance the compensation of any of its employees.

`(F) A requirement for the establishment of a Board Compensation Committee that meets the requirements of subsection (c).

`(4) CERTIFICATION OF COMPLIANCE- The chief executive officer and chief financial officer (or the equivalents thereof) of each TARP recipient shall provide a written certification of compliance by the TARP recipient with the requirements of this section--

`(A) in the case of a TARP recipient, the securities of which are publicly traded, to the Securities and Exchange Commission, together with annual filings required under the securities laws; and

`(B) in the case of a TARP recipient that is not a publicly traded company, to the Secretary.

`(c) Board Compensation Committee-

`(1) ESTABLISHMENT OF BOARD REQUIRED- Each TARP recipient shall establish a Board Compensation Committee, comprised entirely of independent directors, for the purpose of reviewing employee compensation plans.

`(2) MEETINGS- The Board Compensation Committee of each TARP recipient shall meet at least semiannually to discuss and evaluate employee compensation plans in light of an assessment of any risk posed to the TARP recipient from such plans.

`(3) COMPLIANCE BY NON-SEC REGISTRANTS- In the case of any TARP recipient, the common or preferred stock of which is not registered pursuant to the Securities Exchange Act of 1934, and that has received $25,000,000 or less of TARP assistance, the duties of the Board Compensation Committee under this subsection shall be carried out by the board of directors of such TARP recipient.

`(d) Limitation on Luxury Expenditures- The board of directors of any TARP recipient shall have in place a company-wide policy regarding excessive or luxury expenditures, as identified by the Secretary, which may include excessive expenditures on--

`(1) entertainment or events;

`(2) office and facility renovations;

`(3) aviation or other transportation services; or

`(4) other activities or events that are not reasonable expenditures for staff development, reasonable performance incentives, or other similar measures conducted in the normal course of the business operations of the TARP recipient.

<u>(e) PROHIBITION ON EXECUTIVE COMPENSATION NOT BASED ON PERFORMANCE STANDARDS.—</u>

<u>(1) PROHIBITION.—No financial institution that has received or receives a direct capital investment under the Troubled Assets Relief Program under this title, or with respect to the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, or a Federal home loan bank, under the amendments made by section 1117 of the Housing and Economic Recovery Act of 2008, may, while that capital investment remains outstanding, make a compensation payment, other than a longevity bonus or a payment in the form of restricted stock, to any executive or employee under any existing compensation arrangement, or enter into a new compensation payment arrangement, if such compensation payment or compensation payment arrangement—</u>

<u>(A) provides for compensation that is unreasonable or excessive, as defined in standards established by the Secretary, in consultation with the Chairperson of the Congressional Oversight Panel established under section 125, in accordance with paragraph (2); or</u>

<u>(B) includes any bonus, or other supplemental payment that is not directly based on performance-based measures set forth in standards established by the Secretary in accordance with paragraph (2).</u>

<u>Provided that, nothing in this paragraph (e)(1) applies to an institution that did business with a recipient of a direct capital investment under the TARP.</u>

(2) STANDARDS.—Not later than 30 days after the date of enactment of this subsection, the Secretary, in consultation with the Chairperson of the Congressional Oversight Panel established under section 125, with the approval of the agencies that are members of the Federal Financial Institutions Examination Council, shall establish the following:

(A) UNREASONABLE AND EXCESSIVE COMPENSATION STANDARDS.—Standards that define 'unreasonable or excessive' for purposes of subparagraph (1)(A).

(B) PERFORMANCE-BASED STANDARDS.—Standards for performance-based measures that a financial institution must apply when determining whether it may provide a bonus or retention payment under paragraph (1)(B). Such performance measures shall include—

(i) the stability of the financial institution and its ability to repay or begin repaying the United States for any capital investment received under this title;

(ii) the performance of the individual executive or employee to whom the payment relates;

(iii) adherence by executives and employees to appropriate risk management requirements; and

(iv) other standards which provide greater accountability to shareholders and taxpayers.

(3) REPORTING REQUIREMENT. —

(A) IN GENERAL.—Any financial institution that is subject to the requirements of paragraph (1) shall, not later than 90 days after the date of enactment of this subsection and annually on March 31 each year thereafter, transmit to the Secretary, who shall make a report which states how many persons (officers, directors and employees) received or will receive total compensation in that fiscal year in each of the following amounts:

(i) over $500,000;

(ii) over $1,000,000;

(iii) over $2,000,000;

(iv) over $3,000,000; and

(v) over $5,000,000.

The report shall distinguish amounts the institution considers to be a bonus and the reason for such distinction. The name or identity of persons receiving compensation in such amounts shall not be required in such reports. The Secretary shall make such reports available on the Internet. Any financial institution subject to this paragraph shall issue a retrospective annual report for 2008 and both a prospective and retrospective annual report for each subsequent calendar year until such institution ceases to be subject to this paragraph.

(B) TOTAL COMPENSATION DEFINED.—For purposes of this paragraph, the term 'total compensation' includes all cash payments (including without limitation salary, bonus, retention payments), all transfers of property, stock options, sales of stock, and all contributions by the company (or its affiliates) for that person's benefit.

`(f) Shareholder Approval of Executive Compensation-

`(1) ANNUAL SHAREHOLDER APPROVAL OF EXECUTIVE COMPENSATION- Any proxy or consent or authorization for an annual or other meeting of the shareholders of any TARP recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding shall permit a separate shareholder vote to approve the compensation of executives, as disclosed pursuant to the compensation disclosure rules of the Commission (which disclosure shall include the compensation discussion and analysis, the compensation tables, and any related material).

`(2) NONBINDING VOTE- A shareholder vote described in paragraph (1) shall not be binding on the board of directors of a TARP recipient, and may not be construed as overruling a decision by such board, nor to create or imply any additional fiduciary duty by such board, nor shall such vote be construed to restrict or limit the ability of shareholders to make proposals for inclusion in proxy materials related to executive compensation.

`(3) DEADLINE FOR RULEMAKING- Not later than 1 year after the date of enactment of the American Recovery and Reinvestment Act of 2009, the Commission shall issue any final rules and regulations required by this subsection.

`(g) Review of Prior Payments to Executives-

`(1) IN GENERAL- The Secretary shall review bonuses, retention awards, and other compensation paid to the senior executive officers and the next 20 most highly-compensated employees of each entity receiving TARP assistance before the date of enactment of the American Recovery and Reinvestment Act of 2009, to determine whether any such payments were inconsistent with the purposes of this section or the TARP or were otherwise contrary to the public interest.

`(2) NEGOTIATIONS FOR REIMBURSEMENT- If the Secretary makes a determination described in paragraph (1), the Secretary shall seek to negotiate with the TARP recipient and the subject employee for appropriate reimbursements to the Federal Government with respect to compensation or bonuses.

`(h) No Impediment to Withdrawal by TARP Recipients- Subject to consultation with the appropriate Federal banking agency (as that term is defined in section 3 of the Federal Deposit Insurance Act), if any, the Secretary shall permit a TARP recipient to repay any assistance previously provided under the TARP to such financial institution, without regard to whether the financial institution has replaced such funds from any other source or to any waiting period, and when such assistance is repaid, the Secretary shall liquidate warrants associated with such assistance at the current market price.

`(i) Regulations- The Secretary shall promulgate regulations to implement this section.'.

SEC. 7002. APPLICABILITY WITH RESPECT TO LOAN MODIFICATIONS.

Section 109(a) of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5219(a)) is amended--

(1) by striking `To the extent' and inserting the following:

`(1) IN GENERAL- To the extent'; and

(2) by adding at the end the following:

`(2) WAIVER OF CERTAIN PROVISIONS IN CONNECTION WITH LOAN MODIFICATIONS- The Secretary shall not be required to apply executive compensation restrictions under section 111, or to receive warrants or debt instruments under section 113, solely in connection with any loan modification under this section.'.

Speaker of the House of Representatives.

Vice President of the United States and
President of the Senate.

END

IB

Union Calendar No. 20

111TH CONGRESS
1ST SESSION

H. R. 1575

[Report No. 111–50]

To authorize the Attorney General to limit or recover excessive compensation paid or payable by entities that have received Federal financial assistance on or after September 1, 2008.

IN THE HOUSE OF REPRESENTATIVES

MARCH 17, 2009

Mr. CONYERS (for himself, Mr. COHEN, Mr. NADLER of New York, Mr. DELAHUNT, Mr. JOHNSON of Georgia, Mr. PIERLUISI, Ms. FUDGE, and Mr. TONKO) introduced the following bill; which was referred to the Committee on the Judiciary

MARCH 24, 2009

Additional sponsors: Ms. WASSERMAN SCHULTZ, Mr. BOSWELL, Mr. BACA, Ms. JACKSON-LEE of Texas, Ms. ESHOO, Ms. HIRONO, and Mr. SHERMAN

MARCH 24, 2009

Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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A BILL

To authorize the Attorney General to limit or recover excessive compensation paid or payable by entities that have received Federal financial assistance on or after September 1, 2008.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the ''End Government Reimbursement of Excessive Executive Disbursements (End GREED) Act''.

SEC. 2. STATEMENT OF AUTHORITY.

Congress hereby elects to use its authority under article I, section 8, clause 4, and article I, section 8, clause 18, of the Constitution—

(1) to establish a uniform law on bankruptcy that applies to entities that have received extraordinary financial assistance from the United States on or after September 1, 2008, and

(2) to authorize the Attorney General of the United States (hereinafter in this Act referred to as the Attorney General), after consultation with the Secretary of the Treasury (hereinafter in this Act referred to as the Secretary)—

(A) to seek recovery of previous excessive payments of compensation made by such entities after receiving such assistance, and

(B) to limit excessive payments of compensation to be made by such entities.

SEC. 3. RECOVERY OF EXCESSIVE COMPENSATION.

(a) REVIEW OF CONTRACTS AND PAYMENTS.—The Attorney General, after consultation with the Secretary, on behalf of the Government may review any employment contract made by a recipient entity, and any payment made on or after September 1, 2008, by a recipient entity to an employee.

(b) CIVIL ACTION FOR FRAUDULENT TRANSFER.—The Attorney General may commence a civil action in an appropriate district court of the United States to avoid any payment made by a recipient entity to an employee (including a payment under an employment contract) that was made on or after September 1, 2008, if such entity received less than a reasonably equivalent value in exchange for such payment and such entity—

(1) was insolvent on the date that such payment was made, not taking into account any—

(A) line of credit,

(B) loan, or

(C) payment in exchange for stock of such entity,

received by such entity from the United States on or after September 1, 2008, or

(2) was engaged in business or a transaction, or was about to engage in business or a transaction, for

which property remaining in the recipient entity was an unreasonably small capital.

For purposes of this subsection, the Attorney General may avoid any transfer of an interest of a recipient entity in property, or any obligation incurred by such entity, that is avoidable under applicable law by a creditor holding an unsecured claim against such entity.

(c) CIVIL ACTION TO AVOID CONTRACTUAL OBLIGATIONS TO PAY EXCESSIVE COMPENSATION.—The Attorney General may commence a civil action in an appropriate district court of the United States to limit the amount of the compensation paid or payable on or after the date of the enactment of this Act by a recipient entity under an employment contract if such compensation is greater than an amount equal to 10 times the amount of the mean amount of compensation paid or payable to non-management employees of such entity for any purpose during the calendar year in which compensation was paid or payable by such entity.

SEC. 4. SUBPOENA AUTHORITY.

The Attorney General is authorized to issue a subpoena requiring the attendance and testimony of witnesses and the production of documentary evidence relating to any matter relevant to the implementation of this Act, including the circumstances surrounding any employment contract or payment of compensation, which subpoena, in the case of contumacy or refusal to obey, shall be enforceable by order of an appropriate district court of the United States.

SEC. 5. RULE OF CONSTRUCTION.

Other than limiting compensation paid or payable under employment contracts or providing for the recovery of previously paid compensation, nothing in this Act shall be construed to have any impact on a recipient entity, its financial status, or the financial status of its creditors.

SEC. 6. DEFINITIONS.

For purposes of this Act—

(1) the term ''employment contract'' means an employment contract that provides for the payment of compensation (including performance or incentive compensation, a bonus of any kind, or any other financial return designed to replace or enhance incentive, stock, or other compensation), and

(2) the term ''recipient entity'' means a person (including any subsidiary of such person) that receives, during any period beginning on or after September 1, 2008, from the United States—

(A) a line of credit or a loan,

(B) a payment in exchange for stock of such person (or such subsidiary), or

(C) any combination of credit, loans, or payments,

that exceeds $10,000,000,000 in the aggregate.

Union Calendar No. 20

111TH CONGRESS
1ST SESSION

H. R. 1575

[Report No. 111–50]

A BILL

To authorize the Attorney General to limit or recover excessive compensation paid or payable by entities that have received Federal financial assistance on or after September 1, 2008.

MARCH 24, 2009

Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

CLEARY GOTTLIEB

NEW YORK WASHINGTON PARIS BRUSSELS LONDON MOSCOW FRANKFURT COLOGNE ROME MILAN HONG KONG BEIJING

Overview of the Executive Compensation Provisions of the American Recovery and Reinvestment Act of 2009

New York
February 16, 2009

On February 13, 2009, the House of Representatives and the Senate passed the economic stimulus bill (H.R. 1) known as "The American Recovery and Reinvestment Act of 2009." President Obama is expected to sign the bill into law on Tuesday, February 17, 2009. The bill will significantly rewrite the original executive compensation and corporate governance provisions of Section 111 of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5221, "EESA") and will apply to all institutions that have received or will receive financial assistance under the Troubled Asset Relief Program ("TARP"). Among the most important changes instituted by the bill are new limits on the ability of TARP recipients to pay incentive compensation to up to 20 of the next most highly-compensated employees in addition to their "senior executive officers," a prohibition on termination of employment payments to senior executive officers and the five next most highly-compensated employees and a requirement that TARP recipients implement "say on pay" shareholder votes.

This memorandum briefly outlines Section 111 of EESA as it would be revised. The relevant legislative text is contained in Division B – Title VII of the bill. The legislation and authorities cited are attached to this memorandum and may be viewed in electronic form by clicking the links provided in this memorandum or the tabs to the left of the page.

- Covered Entities. EESA §111 would apply to "TARP Recipients," meaning any entity that ***has received or will receive financial assistance*** under TARP. We presume that the rule concerning controlled group aggregation in Q&A 1 in the Interim Final Rule issued by the Department of the Treasury ("Treasury") relating to the TARP Capital Purchase Program (the "Interim Final Rule") would apply. As described below, EESA §111(g) also would include a provision that loosens the standards under which an entity that chose to participate in TARP could repay the funds received by it in order to limit the application of EESA §111 to it.
    - Currently, TARP includes the following programs: Capital Purchase Program, Systemically Significant Failing Institutions Program, Targeted Investment Program, Automotive Industry Financing Program, Term Asset-Backed Securities Loan Facility and the Treasury's recently announced Capital Assistance Program.
- Covered Period. EESA §111, in general, would apply while any obligation arising from financial assistance under TARP is outstanding, excluding warrants to purchase common

stock of the TARP Recipient. EESA §111(h) requires the Secretary of the Treasury (the "Secretary") to promulgate regulations to implement EESA §111, and the Securities and Exchange Commission (the "SEC") to issue regulations concerning the new "say on pay" requirement as described below. Since some provisions would require more or less immediate action by some TARP Recipients (such as, for example, "say on pay" proxy proposals, CEO and CFO certifications, and certain compensation decisions), it seems likely that quick guidance will be provided concerning whether compliance is required prior to the promulgation of regulations.

- Covered Employees. There are four provisions that apply to certain highly-compensated employees of the TARP Recipient in addition to the five "senior executive officers" or "SEOs." These provisions require a determination of the Top 5, Top 10 or Top 20 most highly-compensated employees other than the SEOs. These determinations raise several questions not addressed by the legislation:

    - Controlled Group. There is no express provision requiring that all employees of the controlled group be taken into account in making this determination, unless the Treasury adopts a controlled group aggregation rule similar to that in Q&A 1 in the Interim Final Rule.

    - Measurement of Compensation. There is also no specific rule dictating the method by which the next most highly-compensated employees will be determined. An SEO is defined as an "individual who is 1 of the top 5 most highly paid executives of a public company, whose compensation is required to be disclosed pursuant to the Securities Exchange Act of 1934, and any regulations issued thereunder, and non-public company counterparts." EESA §111(a)(1). For purposes of determining the SEOs, therefore, EESA §111 uses compensation as reported in the TARP Recipient's annual meeting proxy statement or Annual Report on Form 10-K. It is unclear whether the same rules will be used to determine the compensation of non-executive employees. In addition, the statute does not define the measurement period for determining compensation. For purposes of Section 162(m)(5) of the Internal Revenue Code of 1986, as amended (the "Code"), the determination is based on the year for which the deduction would be taken (the "current year method") as reported in the proxy statement or Form 10-K filed after the end of the year. See Frequently Asked Questions issued by the Treasury in January 2009 (the "January FAQs"). For purposes of the other provisions of the Capital Purchase Program, the determination of the affected SEOs for a year is based on compensation in the prior year (the "look back method"). Both methods are problematical when used to determine which employees' compensation will be limited as required by EESA §111 as it is proposed to be revised. If the current year method is used, the application of the limitation itself potentially affects the identity of the covered employees in a circular fashion. If the look back method is used, the identity of the covered employees would presumably alternate every year.

- Prohibition on Golden Parachutes. No "golden parachute" would be permitted to be paid to an SEO or any of the next five most highly-compensated employees of any TARP Recipient.

EESA §111(b)(3)(C). A golden parachute is an amount payable "for departure from a company for ***any*** reason (emphasis added), except for payments for services performed or benefits accrued." EESA §111(a)(2).

- The reference to the next five most highly-compensated employees is not limited to executive officers and can include traders, commission salespersons and investment bankers.

- Based on the January FAQs, this prohibition would apply to payments after all TARP obligations are repaid if the departure occurs during the period any such obligations were outstanding (other than warrants).

- The scope of this prohibition is unclear. Read literally, it would include payments for terminations of employment resulting from death or disability. Based on prior guidance issued by the Treasury, the provision may be interpreted to prohibit any accelerated vesting of stock or option awards. See Q&A 9(c)(1) in the Interim Final Rule.

- The scope of the exceptions for "benefits accrued" and for "payments for services performed" is also unclear. For example, would accrual for accounting purposes be sufficient or would some other standard, such as a vesting requirement or the principles underlying an accrued benefit in the tax-qualified plan rules, apply?

- Prohibition on Bonus, Retention and Incentive Compensation. No bonus, retention award or incentive compensation, other than restricted stock meeting certain requirements, would be permitted to be paid or accrued by a TARP Recipient with respect to covered individuals. EESA §111(b)(3)(D)(ii). The number and identity of covered employees subject to this restriction would vary as follows, based on the amount of TARP assistance received by the TARP Recipient:

Amount of Financial Assistance Received under TARP	**Covered Employees**
Less than $25 million	The most highly-compensated employee (HCE)
$25 - $250 million	Top 5 HCEs
$250 - $500 million	SEOs + Top 10 HCEs
$500 million or more	SEOs + Top 20 HCEs
The Secretary may subject employees in addition to the 5, 10 and 20 above to this requirement as it deems to be in the public interest.	

- A grant of restricted stock would be permitted if it (1) does not fully vest during the period that any TARP obligation (other than warrants) is outstanding, (2) does not have a value greater than 1/3 of total annual compensation of the employee receiving the grant and (3) is subject to any other terms and conditions as the Secretary may determine is in the public interest. (The terms "total annual compensation" and "fully vest" are not defined.)

   - There is an exception for bonus payments required to be paid pursuant to written employment contracts executed on or before February 11, 2009, "as such valid employment contracts are determined by the Secretary or the designee of the Secretary." The ability to rely upon this exception absent such determination, as well as the process of such determination, is not clear.

   - EESA §111 would not limit the amount of salary or other vested non-incentive compensation (such as, for example, pensions) permitted to be paid by TARP Recipients. This provision will have unintended consequences that benefit neither the Treasury nor the TARP Recipient and its shareholders. In some cases, it will encourage TARP Recipients to increase their reliance on vested non-incentive compensation to attract and retain employees. In other cases, it will encourage employees to defect to less regulated competitors or for TARP Recipients to spin off adversely affected operations.

   - There is no exception for compensation paid in the form of restricted stock units, which can be economically identical to shares of restricted stock, or stock options.

- Risk Evaluation. TARP Recipients would be required to establish limits on compensation in order to exclude incentives that encourage unnecessary and excessive risk taking. EESA §§111(b)(2) and (3)(A).

- Clawback Requirement. TARP Recipients would be required to provide for the recovery of any bonus, retention or incentive awards paid to any SEO or any of the next 20 most highly-compensated employees based on materially inaccurate earnings, revenues, gains or other criteria. EESA §111(b)(3)(B).

- Anti-Manipulation Protection. TARP Recipients would be required to prohibit compensation plans that would encourage manipulation of reported earnings in order to enhance compensation of any employee. EESA §111(b)(3)(E).

- CEO and CFO Certifications. The CEO and CFO of each TARP Recipient would be required to provide a written certification of compliance with the new executive compensation provisions to the SEC in the TARP Recipient's annual filings (for public companies) and to the Secretary (for non-public companies). EESA §111(b)(4).

   - While not clear, the public company certification may be required in the upcoming proxy statement or Annual Report on Form 10-K. TARP Recipients may, therefore, wish to quickly consider what internal mechanics should be implemented to support these certifications.

- Compensation Committee Requirements. TARP Recipients would be required to establish (or, presumably, to continue to provide for) a board compensation committee of independent directors to review employee compensation plans. The committee would be required to meet at least semiannually to discuss and evaluate risks posed to the TARP Recipient by its compensation plans. For non-public TARP Recipients that received $25 million or less of TARP assistance, the board of directors as a whole would be permitted to carry out these duties. EESA §111(c).

- Policy on Excessive or Luxury Expenditures. The board of directors of each TARP Recipient would be required to adopt a company-wide policy on excessive or luxury expenditures, including on entertainment, office and facility renovations, aviation and other transportation, and other activities or events that are not reasonable expenditures for staff development, performance incentives or similar measures in the ordinary course of business operations. EESA §111(d).

- "Say on Pay" Voting. Each TARP Recipient would be required to provide for a non-binding say on pay shareholder vote to approve compensation of executives as disclosed pursuant to SEC rules (including the Compensation Disclosure &Analysis, compensation tables and related material). EESA §111(e).

    - Read literally, this requirement would apply to annual meetings occurring after the date of enactment of new EESA §111. However, the legislation gives the SEC one year to promulgate any final regulations required by this provision. It is not clear whether the say on pay vote would be required to be implemented prior to the issuance of such final regulations.

- Secretary of the Treasury Review of Compensation Plans. The Secretary would be required to review bonuses, retention awards and other compensation paid prior to enactment of the new law to the SEOs and the next 20 most highly-compensated employees of TARP Recipients in order to determine whether such payments were inconsistent with the purposes of EESA §111 or TARP or were otherwise contrary to public interest and, if appropriate, negotiate reimbursement with the TARP Recipient and the employee. EESA §111(f).

- Section 162(m) Deductibility Cap. Each TARP Recipient will be subject to the provisions of Section 162(m)(5) of the Code, "as applicable." EESA §111(b)(1)(B). Section 162(m)(5) prevents a tax deduction to be taken by an "applicable employer" in any year in excess of $500,000 for compensation paid to any SEO, with no exception for performance-based compensation. As drafted, an "applicable employer" includes an entity from which Treasury acquires an aggregate amount of troubled assets exceeding $300 million in auction (not direct) purchases.

    - Given the shift in approach by Treasury since EESA was originally passed from purchases of troubled assets themselves (whether directly or by auction) to direct investment in equity of financial institutions, it is not clear whether the new legislation means to expand the application of Section 162(m)(5) to TARP Recipients in current TARP programs not involving auction purchases. While not clear, it could be read to pick up TARP Recipients of over $300 million in any type of financial assistance under TARP.

- Repayment of TARP Funds. Subject to consultation with the appropriate Federal banking agency, a TARP Recipient may repay financial assistance previously provided under TARP without regard to replacement of the funds from any other source or any waiting period. Upon repayment, any warrants held by the Treasury would be liquidated at the current market price. EESA §111(g).
    - If a financial institution were to repay, each of the foregoing requirements would need to be reviewed with regard to how they might apply to any partial year.

On February 4, 2009, the Treasury also announced New Restrictions on Executive Compensation for participants in generally available capital access programs as well as those financial institutions in need of exceptional financial recovery assistance. Those guidelines applied to entities receiving assistance in the future. The extent to which these restrictions would be superseded by new EESA §111 is unclear. Some of those guidelines would merely be codified by new EESA §111, such as the certification requirement and the luxury expenses policy. Other requirements, such as the $500,000 annual compensation limit for SEOs and changes to the "golden parachute" and "clawback" provisions, presumably would be superseded.

Please contact A. Richard Susko, Arthur H. Kohn or Mary E. Alcock, or any of your other regular contacts at the firm, for further information about the matters discussed above.

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and Information Administration in a form that is interactive and searchable.

(m) The Assistant Secretary shall have the authority to prescribe such rules as are necessary to carry out the purposes of this section.

TITLE VII—LIMITS ON EXECUTIVE COMPENSATION

SEC. 7000. TABLE OF CONTENTS.

The table of contents of this title is as follows:

TITLE VII—LIMITS ON EXECUTIVE COMPENSATION

SEC. 7001. EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.

Section 111 of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5221) is amended to read as follows:

"SEC. 111. EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.

"(a) DEFINITIONS.—For purposes of this section, the following definitions shall apply:

"(1) SENIOR EXECUTIVE OFFICER.—The term 'senior executive officer' means an individual who is 1 of the top 5 most highly paid executives of a public company, whose compensation is required to be disclosed pursuant to the Securities Exchange Act of

1934, and any regulations issued thereunder, and non-public company counterparts.

"(2) GOLDEN PARACHUTE PAYMENT.—The term 'golden parachute payment' means any payment to a senior executive officer for departure from a company for any reason, except for payments for services performed or benefits accrued.

"(3) TARP RECIPIENT.—The term 'TARP recipient' means any entity that has received or will receive financial assistance under the financial assistance provided under the TARP.

"(4) COMMISSION.—The term 'Commission' means the Securities and Exchange Commission.

"(5) PERIOD IN WHICH OBLIGATION IS OUTSTANDING; RULE OF CONSTRUCTION.—For purposes of this section, the period in which any obligation arising from financial assistance provided under the TARP remains outstanding does not include any period during which the Federal Government only holds warrants to purchase common stock of the TARP recipient.

"(b) EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.—

"(1) ESTABLISHMENT OF STANDARDS.—During the period in which any obligation arising from financial assistance provided under the TARP remains outstanding, each TARP recipient shall be subject to—

"(A) the standards established by the Secretary under this section; and

"(B) the provisions of section 162(m)(5) of the Internal Revenue Code of 1986, as applicable.

"(2) STANDARDS REQUIRED.—The Secretary shall require each TARP recipient to meet appropriate standards for executive compensation and corporate governance.

"(3) SPECIFIC REQUIREMENTS.—The standards established under paragraph (2) shall include the following:

"(A) Limits on compensation that exclude incentives for senior executive officers of the TARP recipient to take unnecessary and excessive risks that threaten the value of such recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding.

"(B) A provision for the recovery by such TARP recipient of any bonus, retention award, or incentive compensation paid to a senior executive officer and any of the next 20 most highly-compensated employees of the TARP recipient based on statements of earnings, revenues, gains, or other criteria that are later found to be materially inaccurate.

"(C) A prohibition on such TARP recipient making any golden parachute payment to a senior executive officer or any of the next 5 most highly-compensated employees of the TARP recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding.

"(D)(i) A prohibition on such TARP recipient paying or accruing any bonus, retention award, or incentive compensation during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding, except that any prohibition developed under this paragraph shall not apply to the payment of long-term restricted stock by such TARP recipient, provided that such long-term restricted stock—

"(I) does not fully vest during the period in which any obligation arising from financial assistance provided to that TARP recipient remains outstanding;

"(II) has a value in an amount that is not greater than ⅓ of the total amount of annual compensation of the employee receiving the stock; and

"(III) is subject to such other terms and conditions as the Secretary may determine is in the public interest.

"(ii) The prohibition required under clause (i) shall apply as follows:

"(I) For any financial institution that received financial assistance provided under the TARP equal to less than $25,000,000, the prohibition shall apply only to the most highly compensated employee of the financial institution.

"(II) For any financial institution that received financial assistance provided under the TARP equal to at least $25,000,000, but less than $250,000,000, the prohibition shall apply to at least the 5 most highly-compensated employees of the financial institution, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

"(III) For any financial institution that received financial assistance provided under the TARP equal to at least$250,000,000, but less than $500,000,000, the prohibition shall apply to the senior executive officers and at least the 10 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

"(IV) For any financial institution that received financial assistance provided under the TARP equal to $500,000,000 or more, the prohibition shall apply to the senior executive officers and at least the 20 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

"(iii) The prohibition required under clause (i) shall not be construed to prohibit any bonus payment required to be paid pursuant to a written employment contract executed on or before

February 11, 2009, as such valid employment contracts are determined by the Secretary or the designee of the Secretary.

"(E) A prohibition on any compensation plan that would encourage manipulation of the reported earnings of such TARP recipient to enhance the compensation of any of its employees.

"(F) A requirement for the establishment of a Board Compensation Committee that meets the requirements of subsection (c).

"(4) CERTIFICATION OF COMPLIANCE.—The chief executive officer and chief financial officer (or the equivalents thereof) of each TARP recipient shall provide a written certification of compliance by the TARP recipient with the requirements of this section—

"(A) in the case of a TARP recipient, the securities of which are publicly traded, to the Securities and Exchange Commission, together with annual filings required under the securities laws; and

"(B) in the case of a TARP recipient that is not a publicly traded company, to the Secretary.

"(c) BOARD COMPENSATION COMMITTEE.—

"(1) ESTABLISHMENT OF BOARD REQUIRED.— Each TARP recipient shall establish a Board Compensation Committee, comprised entirely of independent directors, for the purpose of reviewing employee compensation plans.

"(2) MEETINGS.—The Board Compensation Committee of each TARP recipient shall meet at least semiannually to discuss and evaluate employee compensation plans in light of an assessment of any risk posed to the TARP recipient from such plans.

"(3) COMPLIANCE BY NON-SEC REGISTRANTS.—In the case of any TARP recipient, the common or preferred stock of which is not registered pursuant to the Securities Exchange Act of 1934, and that has received $25,000,000 or less of TARP assistance, the duties of the Board Compensation Committee under this subsection shall be carried out by the board of directors of such TARP recipient.

"(d) LIMITATION ON LUXURY EXPENDITURES.—The board of directors of any TARP recipient shall have in place a company-wide policy regarding excessive or luxury expenditures, as identified by the Secretary, which may include excessive expenditures on—

"(1) entertainment or events;

"(2) office and facility renovations;

"(3) aviation or other transportation services; or

"(4) other activities or events that are not reasonable expenditures for staff development, reasonable performance incentives, or other similar measures conducted in the normal course of the business operations of the TARP recipient.

"(e) SHAREHOLDER APPROVAL OF EXECUTIVE COMPENSATION.—

"(1) ANNUAL SHAREHOLDER APPROVAL OF EXECUTIVE COMPENSATION.—Any proxy or consent or authorization for an annual or other meeting of the shareholders of any TARP recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding shall permit a separate shareholder vote to approve the compensation of executives, as disclosed pursuant to the compensation disclosure rules of the Commission (which disclosure shall include the compensation discussion and analysis, the compensation tables, and any related material).

"(2) NONBINDING VOTE.—A shareholder vote described in paragraph (1) shall not be binding on the board of directors of a TARP recipient, and may not be construed as overruling a decision by such board, nor to create or imply any additional fiduciary duty by such board, nor shall such vote be construed to restrict or limit the ability of shareholders to make proposals for inclusion in proxy materials related to executive compensation.

"(3) DEADLINE FOR RULEMAKING.—Not later than 1 year after the date of enactment of the American Recovery and Reinvestment Act of 2009, the Commission shall issue any final rules and regulations required by this subsection.

"(f) REVIEW OF PRIOR PAYMENTS TO EXECUTIVES.—

"(1) IN GENERAL.—The Secretary shall review bonuses, retention awards, and other compensation paid to the senior executive officers and the next 20 most highly-compensated employees of each entity receiving TARP assistance before the date of enactment of the American Recovery and Reinvestment Act of 2009, to determine whether any such payments were inconsistent with the purposes of this section or the TARP or were otherwise contrary to the public interest.

"(2) NEGOTIATIONS FOR REIMBURSEMENT.—If the Secretary makes a determination described in paragraph (1), the Secretary shall seek to negotiate with the TARP recipient and the subject employee for appropriate reimbursements to the Federal Government with respect to compensation or bonuses.

"(g) NO IMPEDIMENT TO WITHDRAWAL BY TARP RECIPIENTS.—Subject to consultation with the appropriate Federal banking agency (as that term is defined in section 3 of the Federal Deposit Insurance Act), if any, the Secretary shall permit a TARP recipient to repay any assistance previously provided under the TARP to such financial institution, without regard to whether the financial institution has replaced such funds from any other source or to any waiting period, and when such assistance is repaid, the Secretary shall liquidate warrants associated with such assistance at the current market price.

"(h) REGULATIONS.—The Secretary shall promulgate regulations to implement this section.".

SEC. 7002. APPLICABILITY WITH RESPECT TO LOAN MODIFICATIONS.

Section 109(a) of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5219(a)) is amended—

(1) by striking "To the extent" and inserting the following:

"(1) IN GENERAL.—To the extent"; and

(2) by adding at the end the following:

"(2) WAIVER OF CERTAIN PROVISIONS IN CONNECTION WITH LOAN MODIFICATIONS.—The Secretary shall not be required to apply executive compensation restrictions under section 111, or to receive warrants or debt instruments under section 113, solely in connection with any loan modification under this section.".

Billing Code 4810-25-P

DEPARTMENT OF THE TREASURY

Domestic Finance

31 CFR Part 30

TARP CAPITAL PURCHASE PROGRAM

AGENCY: Domestic Finance, Treasury.

ACTION: Interim final rule.

SUMMARY: This interim rule, promulgated pursuant to sections 101(a)(1), 101(c)(5), and 111(b) of the Emergency Economic Stabilization Act of 2008, Division A of Public Law 110-343 (EESA), provides guidance on the executive compensation provisions applicable to participants in the Troubled Assets Relief Program (TARP) Capital Purchase Program (CPP). Section 111(b) of EESA requires financial institutions from which the Department of the Treasury (Treasury) is purchasing troubled assets through direct purchases to meet appropriate standards for executive compensation and corporate governance. This interim final rule includes the following standards for purposes of the CPP: (a) limits on compensation that exclude incentives for senior executive officers

(SEOs) of financial institutions to take unnecessary and excessive risks that threaten the value of the financial institution; (b) required recovery of any bonus or incentive compensation paid to a SEO based on statements of earnings, gains, or other criteria that are later proven to be materially inaccurate; (c) prohibition on the financial institution from making any golden parachute payment to any SEO; and (d) agreement to limit a claim to a federal income tax deduction for certain executive remuneration. These rules generally affect financial institutions that participate in the CPP, certain employers related to those financial institutions, and their officers.

DATES: Effective Date: These regulations are effective on [**INSERT DATE OF PUBLICATION IN THE FEDERAL REGISTER**]. Comment due date: [**INSERT DATE THAT IS THIRTY DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER**].

ADDRESSES: The Treasury requests comments on the topics addressed in this interim rule. Comments may be submitted to the Treasury by any of the following methods: Submit electronic comments through the federal government e-rulemaking portal, www.regulations.gov or by email to executivecompensationcomments@do.treas.gov or send paper comments in triplicate to Executive Compensation Comments, Office of Financial Institutions Policy, Room 1418, Department of the Treasury, 1500 Pennsylvania Avenue, NW, Washington, DC 20220.

In general, the Treasury will post all comments to www.regulations.gov without change, including any business or personal information provided such as names, addresses, e-mail addresses, or telephone numbers. The Treasury will also make such comments available for public inspection and copying in the Treasury's Library, Room 1428, Main Department Building, 1500 Pennsylvania Avenue, NW, Washington, DC 20220, on official business days between the hours of 10:00 a.m. and 5:00 p.m. Eastern Time. You can make an appointment to inspect comments by telephoning (202) 622-0990. All comments, including attachments and other supporting materials, received are part of the public record and subject to public disclosure. You should submit only information that you wish to make available publicly.

FOR FURTHER INFORMATION CONTACT: For further information regarding this interim rule contact the Office of Domestic Finance, the Treasury, at (202) 927-6618.

SUPPLEMENTARY INFORMATION:

I. Background.

This document adds 31 CFR Part 30 under section 111(b) of the Emergency Economic Stabilization Act of 2008, Div. A of Pub. Law No. 110-343 (EESA) with respect to the Troubled Assets Relief Program (TARP) Capital Purchase Program (CPP) established by the Department of the Treasury (Treasury) under EESA. Section 101(a) of EESA authorizes the Secretary of the Treasury to establish a TARP to "purchase, and to make and fund commitments to purchase, troubled assets from any financial institution, on such terms and conditions as are determined by the Secretary, and in accordance with this Act and policies and procedures developed and published by the Secretary." Section

120 of EESA provides that the TARP authorities generally terminate on December 31, 2009, unless extended upon certification by the Secretary of the Treasury to Congress, but in no event later than two years from the date of enactment of EESA (October 3, 2008) (the TARP authorities period). Thus, the TARP authorities period is the period from October 3, 2008 to December 31, 2009 or, if extended, the period from October 3, 2008 to the date so extended, but not later than October 3, 2010.

Section 111 of EESA provides that certain financial institutions that sell assets to the Treasury may be subject to specified executive compensation standards. In the case of auction purchases from a financial institution that has sold assets in an amount that exceeds $300 million in the aggregate (including direct purchases), the financial institution is prohibited under section 111(c) of EESA from entering into any new employment contract with a senior executive officer (SEO) that provides a golden parachute to the SEO in the event of the SEO's involuntary termination, or in connection with the financial institution's bankruptcy filing, insolvency, or receivership. This prohibition applies during the TARP authorities period. The Treasury has issued separate guidance on this provision (Notice 2008-TAAP).

In addition, for auction purchases, section 302 of EESA includes tax provisions as amendments to sections 162(m) and 280G of the Internal Revenue Code (26 U.S.C. 162(m) and 280G) that address compensation paid to certain executive officers employed by financial institutions that sell assets under TARP. Section 302(a) of EESA amended 26 U.S.C. 162(m) to add a new paragraph (m)(5), which reduces the deduction limit to $500,000 in the case of “executive remuneration” and “deferred deduction executive remuneration.” This limit applies only to certain employers participating in an auction purchase and only for certain taxable years. Employers covered under 26 U.S.C. 162(m)(5) are not limited to publicly held corporations (nor even to corporations). The exception for performance-based compensation and certain other exceptions do not apply in the case of executive compensation covered under 26 U.S.C. 162(m)(5). The Treasury and the Internal Revenue Service have issued guidance on these provisions (I.R.S. Notice 2008-94).

In the case of direct purchases, section 111(b)(1) of EESA requires financial institutions to meet appropriate standards for executive compensation and corporate governance as set forth by the Secretary of the Treasury. These standards apply to the SEOs of the financial institutions while the Treasury holds an equity or debt position in the financial institution acquired under the CPP. Section 111(b)(2) of EESA requires that at least three criteria be satisfied by financial institutions from which the Treasury directly purchases troubled assets and takes a meaningful equity or debt position. The following describes these criteria.

Section 111(b)(2)(A) of EESA requires “limits on compensation that exclude incentives for senior executive officers of a financial institution to take unnecessary and excessive risks that threaten the value of the financial institution during the period that the Secretary holds an equity or debt position in the financial institution.”

Section 111(b)(2)(B) of EESA requires “a provision for the recovery by the financial institution of any bonus or incentive compensation paid to a senior executive officer based on statements of earnings, gains, or other criteria that are later proven to be materially inaccurate.”

Section 111(b)(2)(C) of EESA requires “a prohibition on the financial institution making any golden parachute payment to its senior executive officer during the period that the Secretary holds an equity or debt position in the financial institution.”

Treasury Notice 2008-PSSFI addresses these provisions under section 111(b) of EESA as they apply to financial institutions participating in programs for systemically significant failing institutions. Further guidance will be issued for any additional programs.

These regulations are being issued as interim final regulations to implement the purpose of EESA, which is to provide immediately authority and facilities that the Secretary of the Treasury can use to restore liquidity and stability to the financial system of the United States. Thus, to encourage financial institutions to choose to participate in the CPP, these regulations provide those institutions with information with respect to the applicable executive compensation and corporate governance rules that will apply under the CPP.

II. This Interim Rule.

These interim final regulations provide guidance on the executive compensation and corporate governance provisions of section 111(b) of EESA with respect to the CPP. They are written in question and answer format.

The regulations clarify that the requirements of section 111(b) of EESA apply not only to the financial institution that participates in the CPP, but also to any other entity in its controlled group. For this purpose, the controlled group rules in section 414(b) and (c) of the Internal Revenue Code (26 U.S.C. 414(b) and (c)) apply, but only taking into account parent-subsidiary relationships, not brother-sister relationships. These tax rules generally base control on an 80-percent ownership basis. Thus, these interim regulations apply to controlled groups in a manner similar to the executive compensation provisions of section 302(a) of EESA, which added 26 U.S.C. 162(m)(5) and 26 U.S.C. 280G(e) to the Internal Revenue Code, providing special tax treatment for executive compensation for employers participating in the TARP. See 26 U.S.C. 162(m)(5)(B)(iii) and 26 U.S.C. 280G(e)(2)(A).

The requirements in section 111(b) apply with respect to certain executive officers identified in § 30.2 (Q-2) of the regulations. The determination of these executive officers is made based on rules similar to those set forth in the federal securities laws and generally apply to the chief executive officer, the chief financial officer, and the three mostly highly compensated executive officers. The three most highly compensated executive officers are determined according to the requirements in Item 402 of Regulation S-K under the federal securities law (17 CFR 229.402) by reference to the total compensation for the last completed fiscal year. Until the compensation data for the current fiscal year are available, the financial institution should make its best efforts to identify the three most highly compensated executive officers for the current fiscal year.

Analogous rules apply to financial institutions that do not have securities registered with the Securities and Exchange Commission (SEC) pursuant to the federal securities laws.

With respect to section 111(b)(2)(A) for purposes of participation in the CPP, the interim final regulations require the financial institution's compensation committee to identify the features in the financial institution's SEO incentive compensation arrangements that could lead SEOs to take unnecessary and excessive risks that could threaten the value of the financial institution. The regulations require that the compensation committee review the SEO incentive compensation arrangements with the financial institution's senior risk officers, or other personnel acting in a similar capacity, to ensure that SEOs are not encouraged to take such risks. The regulations require such review promptly, and in no case more than 90 days, after the purchase under the CPP.

The regulations also require that the compensation committee meet at least annually with the financial institution's senior risk officers to discuss and review the relationship between the financial institution's risk management policies and practices and the SEO incentive compensation arrangements.

In addition, the regulations require the compensation committee to certify that it has completed the reviews of the SEO incentive compensation arrangements as outlined above. Financial institutions with securities registered with the SEC pursuant to the federal securities laws should provide these certifications in the Compensation Discussion and Analysis required pursuant to Item 402(b) of Regulation S-K under the federal securities laws (17 CFR

229.402). Those financial institutions that do not have securities registered with the SEC pursuant to the federal securities laws are required to provide the certifications to their primary regulatory agency.

With respect to section 111(b)(2)(B) of EESA for purposes of participation in the CPP, the interim final regulations provide that the SEO bonus and incentive compensation paid during the period that the Treasury holds an equity or debt position acquired under the CPP must be subject to recovery or "clawback" by the financial institution if the payments were based on materially inaccurate financial statements and any other materially inaccurate performance metric criteria. The regulations include a comparison of this requirement to section 304 of the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley) (Pub. Law No. 107-204).

With respect to section 111(b)(2)(C) of EESA for purposes of participation in the CPP, the interim final regulations prohibit a financial institution from making any golden parachute payment to a SEO during the period the Treasury holds an equity or debt position acquired under the CPP. The regulations define a golden parachute payment in the same way as under 26 U.S.C. 280G as applied with respect to new paragraph (e) of 26 U.S.C. 280G, added by section 302(a) of EESA relating to golden parachute payments. Thus, a golden parachute payment means any payment in the nature of compensation to (or for the benefit of) a SEO made on account of an applicable severance from employment to the extent the aggregate present value of such payments equals or exceeds an amount equal to three times the SEO's base amount. The term "base amount" for a SEO has the meaning set forth in 26 U.S.C. 280G(b)(3) and 26 CFR 1.280G-1, Q&A-34 (except that references to “change in ownership or control” are treated as referring to an “applicable severance from employment”).

The regulations define an applicable severance from employment as any SEO’s severance from employment with the financial institution (i) by reason of involuntary termination of employment with the financial institution or with an entity that is treated as the same employer as the financial institution under the controlled group rules or (ii) in connection with any bankruptcy filing, insolvency, or receivership of the financial institution or of an entity that is treated as the same employer as the financial institution under the controlled group rules. The regulations define an involuntary termination of employment and set forth rules for determining when a payment on account of an applicable severance from employment occurs. These rules are substantially the same as the standards in IRS Notice 2008-94 regarding new paragraph (e) of 26 U.S.C. 280G, and are also generally similar to the pre-existing standards under 26 U.S.C. 280G (see 26 CFR 1.280G-1, Q&A-22(a)).

The regulations include a special rule for cases in which a financial institution (target) that has sold troubled assets to the Treasury through the CPP is acquired by an entity (acquirer) in an acquisition of any form. Under this rule, acquirer does not become subject to section 111(b) of EESA merely as a result of the acquisition. The rule applies only if the acquirer is not related to target and treats target as related if stock or other interests of target are treated (under 26 U.S.C. 318(a) other than paragraph (4) thereof) as owned by acquirer. With respect to target, any employees of target who are SEOs prior to the acquisition will be subject to section 111(b) of EESA until after the first anniversary following the acquisition.

The regulations set forth an additional standard for executive compensation and corporate governance under section 111(b)(1) of EESA. Under this standard, the financial institution must agree, as a condition to participate in the CPP, that no deduction will be claimed for federal income tax purposes for remuneration that would not be deductible if 26 U.S.C. 162(m)(5) were to apply to the financial institution. For this purpose, during the period that the Treasury holds an equity or debt position in the financial institution acquired under the CPP: (i) the financial institution (including entities in its controlled group) is treated as an "applicable employer," (ii) its SEOs are treated as "covered executives," and (iii) any taxable year that includes any portion of that period is treated as an "applicable taxable year," each as defined in 26 U.S.C. 162(m)(5), except that the dollar limitation and the remuneration for the taxable year are prorated for the portion of the taxable year that the Treasury holds an equity or debt position in the financial institution under the CPP. The Secretary has determined that this is an appropriate standard for executive compensation for the CPP. This rule only applies for taxable years that include the period that the Treasury holds an equity or debt position in the financial institution acquired under the CPP. This standard applies even though the financial institution is not subject to 26 U.S.C. 162(m)(5) and only limits the amount of the deduction that may be claimed. Thus, no deduction may be claimed for remuneration during a taxable year for compensation in excess of $500,000 for a SEO, and the special rules relating to deferred deduction executive remuneration would also apply. See I.R.S. Notice 2008-94 for additional information regarding the deduction limit under 26 U.S.C. 162(m)(5).

III. Procedural Requirements.

Justification for Interim Rulemaking

This rule is promulgated pursuant to EESA, the purpose of which is to immediately provide authority and facilities that the Secretary of the Treasury can use to restore liquidity and stability to the financial system of the United States. Specifically, this rule implements certain provisions of section 111 of EESA, which sets forth executive compensation standards for financial institutions that sell troubled assets to the Treasury under EESA. The statute provides that the Secretary may issue guidance and regulations to carry out these provisions and that such guidance and regulations may be effective upon issuance.

In order to encourage financial institutions to choose to participate in the CPP, those institutions must have timely and reliable information with respect to the applicable executive compensation and corporate governance rules that will apply under the program. Accordingly, because EESA authorizes section 111 guidance to be immediately effective and because of exigencies in the financial markets, the Treasury finds that it would be contrary to the public interest, pursuant to 5 U.S.C. 553(b)(B), to delay the issuance of this rule pending an opportunity for public comment and good cause exists to dispense with this requirement. For the same reasons, pursuant to 5 U.S.C. 553(d)(3), the

Treasury has determined that there is good cause for the interim final rule to become effective immediately upon publication. While this regulation is effective immediately upon publication, the Treasury is inviting public comment on the regulation during a thirty-day period and will consider all comments in developing a final rule.

Regulatory Planning and Review

The rule does not meet the criteria for a "significant regulatory action" as defined in Executive Order 12866. Therefore, the regulatory review procedures contained therein do not apply.

Regulatory Flexibility Act

Because no notice of proposed rulemaking is required, this rule is not subject to the provisions of the Regulatory Flexibility Act (5 U.S.C chapter 6).

List of Subjects in 31 CFR Part 30

Executive compensation, Troubled assets.

For the reasons set out in the preamble, Title 31 of the CFR is amended as follows:

PART 30 – TARP CAPITAL PURCHASE PROGRAM

1. Add part 30 to read as follows:

PART 30 – TARP CAPITAL PURCHASE PROGRAM

Sec.
30.0 Executive compensation and corporate governance.
30.1 Q-1: To what financial institutions does this part apply?
30.2 Q-2: Who is a senior executive officer (SEO) under section 111 of EESA?
30.3 Q-3: What actions are necessary for a financial institution participating in the CPP to comply with section 111(b)(2)(A) of EESA?

30.4 Q-4: How should the financial institution comply with the standard under Q&A-3 of this section that the compensation committee, or a committee acting in a similar capacity, review the SEO incentive compensation arrangements to ensure that the SEO incentive compensation arrangements do not encourage the SEOs to take unnecessary and excessive risks that threaten the value of the financial institution?
30.5 Q-5: How should the financial institution comply with the certification requirements under Q&A-3 of this section?
30.6 Q-6: What actions are necessary for a financial institution participating in the CPP to comply with section 111(b)(2)(B) of EESA?
30.7 Q-7: How do the standards under section 111(b)(2)(B) of EESA differ from section 304 of the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley) (Pub. Law No. 107-204)?
30.8 Q-8: What actions are necessary for a financial institution participating in the CPP to comply with section 111(b)(2)(C) of EESA?
30.9 Q-9: What is a golden parachute payment under section 111(b) of EESA?
30.10 Q-10: Are there other conditions that are required under the executive compensation and corporate governance standards in section 111(b)(1) of EESA?
30.11 Q-11: How does section 111(b) of EESA operate in connection with an acquisition, merger, or reorganization?

Authority: Section 111(b) of the Emergency Economic Stabilization Act of 2008, Div. A of Pub. L. 110-343; 122 Stat 3765.

§ 30.0 Executive compensation and corporate governance.

The following questions and answers reflect the executive compensation and corporate governance requirements of section 111(b) of the Emergency Economic Stabilization Act of 2008, Div. A of Pub. Law No. 110-343 (EESA) with respect to participation in the Troubled Assets Relief Program (TARP) Capital Purchase Program (CPP) established by the Treasury thereunder:

§ 30.1 Q-1: To what financial institutions does this part apply?

(a) General rule. This part applies to any financial institution that participates in the CPP.

(b) Controlled group rules. For purposes of section 111(b) of EESA, two or more persons who are treated as a single employer under section 26 U.S.C. 414(b) (employees of a controlled group of corporations) and section 26 U.S.C. 414(c) (employees of partnerships, proprietorships, etc., that are under common control) are treated as a single employer. However, for purposes of section 111(b) of EESA, the rules for brother-sister controlled groups and combined groups are disregarded (including disregarding the rules in section 26 U.S.C. 1563(a)(2) and (a)(3) with respect to corporations and the parallel rules that are in section 26 CFR 1.414(c)-2(c) with respect to other organizations conducting trades or businesses). See § 30.11 (Q-11) of this part for special rules where a financial institution is acquired.

§ 30.2 Q-2: Who is a senior executive officer (SEO) under section 111 of EESA?

(a) General definition. A SEO means a "named executive officer" as defined in Item 402 of Regulation S-K under the federal securities laws (17 CFR 229.402) who: (1) is employed by a financial institution that is participating in the CPP while the Treasury holds an equity or debt position acquired under the CPP; and (2)(i) is the principal executive officer (PEO) (or person acting in a similar capacity) of such financial institution (or, in the case of a controlled group, of the parent entity); (ii) the principal financial officer (PFO) (or person acting in a similar capacity) of such financial institution (or, in the case of a controlled group, of the parent entity); or (iii) one of the three most highly compensated executive officers of such financial institution (or the financial institution's controlled group) other than the PEO or the PFO.

(b) Determination of three most highly compensated executive officers. For financial institutions with securities registered with the Securities and Exchange Commission (SEC) pursuant to the federal securities law, the three most highly compensated executive officers are determined according to the requirements in Item 402 of Regulation S-K under the federal securities laws (17 CFR 229.402). The term "executive officer" has the same meaning as defined in Rule 3b-7 of the Securities Exchange Act of 1934 (Exchange Act) (17 CFR 240.3b-7). For purposes of determining the three most highly compensated executive officers, compensation is determined as it is in Item 402 of Regulation S-K to include total compensation for the last completed fiscal year without regard to whether the compensation is includible in the executive officer's gross income. Until the compensation data for the current fiscal year are available, the financial institution should make its best efforts to identify the three most highly compensated executive officers for the current fiscal year.

(c) Application to private employers. Rules analogous to the rules in paragraphs (a) and (b) of this section apply to financial institutions that are not subject to the federal securities laws, rules, and regulations, including financial institutions that do not have securities registered with the SEC pursuant to the federal securities laws.

§ 30.3 Q-3: What actions are necessary for a financial institution participating in the CPP to comply with section 111(b)(2)(A) of EESA?

In order to comply with section 111(b)(2)(A) of EESA for purposes of participation in the CPP, a financial institution must comply with the following rules: (1) promptly, and in no case more than 90 days, after the purchase under the CPP, the financial institution's compensation committee, or a committee acting in a similar capacity, must review the SEO incentive compensation arrangements with such financial institution's senior risk officers, or other personnel acting in a similar capacity, to ensure that the SEO incentive compensation arrangements do not encourage SEOs to take unnecessary and excessive risks that threaten the value of the financial institution; (2) thereafter, the compensation committee, or a committee acting in a similar capacity, must meet at least annually with senior risk officers, or individuals acting in a similar capacity, to discuss and review the relationship between the financial institution's risk management policies and practices and the SEO incentive compensation arrangements; and (3) the compensation committee, or a committee acting in a similar capacity, must certify that it has completed the reviews of the SEO incentive compensation arrangements required under (1) and (2) above. These rules apply while the Treasury holds an equity or debt position acquired under the CPP.

§ 30.4 Q-4: How should the financial institution comply with the standard under Q-3 of this section that the compensation committee, or a committee acting in a similar capacity, review the SEO incentive compensation arrangements to ensure that the SEO incentive compensation

arrangements do not encourage the SEOs to take unnecessary and excessive risks that threaten the value of the financial institution?

Because each financial institution faces different material risks given the unique nature of its business and the markets in which it operates, the compensation committee, or a committee acting in a similar capacity, should discuss with the financial institution's senior risk officers, or other personnel acting in a similar capacity, the risks (including long-term as well as short-term risks) that such financial institution faces that could threaten the value of the financial institution. The compensation committee, or a committee acting in a similar capacity, should identify the features in the financial institution's SEO incentive compensation arrangements that could lead SEOs to take such risks. Any such features should be limited in order to ensure that the SEOs are not encouraged to take risks that are unnecessary or excessive.

§ 30.5 Q-5: How should the financial institution comply with the certification requirements under Q-3 of this section?

(a) Certification. The compensation committee, or a committee acting in a similar capacity, of the financial institution must provide the certifications required by § 30.3 (Q-3) stating that it has reviewed, with such financial institution's senior risk officers, the SEO incentive compensation arrangements to ensure that the incentive compensation arrangements do not encourage SEOs to take unnecessary and excessive risks. Providing a statement similar to the following and in the manner provided in subparagraphs (b) and (c) of this section, as applicable, would satisfy this standard: "The compensation committee certifies that it has reviewed with senior risk officers the SEO incentive compensation arrangements and has made reasonable efforts to ensure that such arrangements do not encourage SEOs to take unnecessary and excessive risks that threaten the value of the financial institution."

(b) Location. For financial institutions with securities registered with the SEC pursuant to the federal securities law, the compensation committee, or a committee acting in a similar capacity, should provide this certification in the Compensation Discussion and Analysis required pursuant to Item 402(b) of Regulation S-K under the federal securities laws (17 CFR 229.402).

(c) Application to private financial institutions. The rules provided in this section are also applicable to financial institutions that are not subject to the federal securities laws, rules, and regulations, including financial institutions that do not have securities registered with the SEC pursuant to the federal securities laws. A private financial institution should file the certification of the compensation committee, or a committee acting in a similar capacity, with its primary regulatory agency.

§ 30.6 Q-6: What actions are necessary for a financial institution participating in the CPP to comply with section 111(b)(2)(B) of EESA?

In order to comply with section 111(b)(2)(B) of EESA for purposes of participation in the CPP, a financial institution must require that SEO bonus and incentive compensation paid during the period that the Treasury holds an equity or debt position acquired under the CPP are subject to recovery or "clawback" by the financial institution if the payments were based on materially inaccurate financial statements or any other materially inaccurate performance metric criteria.

§ 30.7 Q-7: How do the standards under section 111(b)(2)(B) of EESA differ from section 304 of the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley) (Pub. Law No. 107-204)?

Section 304 of Sarbanes-Oxley requires the forfeiture by a public company's chief executive officer and the chief financial officer of any bonus, incentive-based compensation, or equity-based compensation received and any profits from sales of the company's securities during the twelve-month period following a materially non-compliant financial report. Section 111(b)(2)(B) of EESA differs from section 304 of Sarbanes-Oxley in several ways. The standard under section 111(b)(2)(B) of EESA: applies to the three most highly compensated executive officers in addition to the PEO and the PFO; applies to both public and private financial institutions; is not exclusively triggered by an accounting restatement; does not limit the recovery period; and covers not only material inaccuracies relating to financial reporting but also material inaccuracies relating to other performance metrics used to award bonuses and incentive compensation.

§ 30.8 Q-8: What actions are necessary for a financial institution participating in the CPP to comply with section 111(b)(2)(C) of EESA?

In order to comply with section 111(b)(2)(C) of EESA for purposes of participation in the CPP, a financial institution must prohibit any golden parachute payment to a SEO during the period the Treasury holds an equity or debt position acquired under the CPP.

§ 30.9 Q-9: What is a golden parachute payment under section 111(b) of EESA?

(a) Definition. As provided under 26 U.S.C. 280G(e), a "golden parachute payment" means any payment in the nature of compensation to (or for the benefit of) a SEO made on account of an applicable severance from employment to the extent the aggregate present value of such payments equals or exceeds an amount equal to three times the SEO's base amount. The term "base amount" for a SEO has the meaning set forth in 26 U.S.C. 280G(b)(3) and 26 CFR 1.280G-1, Q&A-34, except that references to "change in ownership or control" are treated as referring to an "applicable severance from employment."

(b) Applicable severance from employment. (1) Definition. An applicable severance from employment means any SEO's severance from employment with the financial institution (i) by reason of involuntary termination of employment with the financial institution or with an entity that is treated as the same employer as the financial institution under § 30.1 (Q-1) of this part; or (ii) in connection with any bankruptcy filing, insolvency, or receivership of the financial institution or of an entity that is treated as the same employer as the financial institution under § 30.1 (Q-1) of this part.

(2) Involuntary termination. (i) An involuntary termination from employment means a termination from employment due to the independent exercise of the unilateral authority of the employer to terminate the SEO's

services, other than due to the SEO's implicit or explicit request to terminate employment, where the SEO was willing and able to continue performing services. An involuntary termination from employment may include the financial institution's failure to renew a contract at the time such contract expires, provided that the SEO was willing and able to execute a new contract providing terms and conditions substantially similar to those in the expiring contract and to continue providing such services. In addition, a SEO's voluntary termination from employment constitutes an involuntary termination from employment if the termination from employment constitutes a termination for good reason due to a material negative change in the SEO's employment relationship. See 26 CFR 1.409A-1(n)(2).

(ii) A severance from employment by a SEO is by reason of involuntary termination even if the SEO has voluntarily terminated employment in any case where the facts and circumstances indicate that absent such voluntary termination the financial institution would have terminated the SEO's employment and the SEO had knowledge that he or she would be so terminated.

(c) Payments on account of an applicable severance from employment. (1) Definition. A payment on account of an applicable severance from employment means a payment that would not have been payable if no applicable severance from employment had occurred (including amounts that would otherwise have been forfeited if no applicable severance from employment had occurred) and amounts that are accelerated on account of the applicable severance from employment. See 26 CFR 1.280G-1, Q&A-24(b), for rules regarding the determination of the amount that is on account of an acceleration.

(2) Excluded amounts. Payments on account of an applicable severance from employment do not include amounts paid to a SEO under a tax qualified retirement plan.

§ 30.10 Q-10: Are there other conditions that are required under the executive compensation and corporate governance standards in section 111(b)(1) of EESA?

The financial institution must agree, as a condition to participate in the CPP, that no deduction will be claimed for federal income tax purposes for remuneration that would not be deductible if 26 U.S.C. 162(m)(5) were to apply to the financial institution. For this purpose, during the period that the Treasury holds an equity or debt position in the financial institution acquired under the CPP: (i) the financial institution (including entities in its controlled group) is treated as an “applicable employer,” (ii) its SEOs are treated as “covered executives,” and (iii) any taxable year that includes any portion of that period is treated as an “applicable taxable year,” each as defined in 26 U.S.C. 162(m)(5), except that the dollar limitation and the remuneration for the taxable year are prorated for the portion of the taxable year that the Treasury holds an equity or debt position in the financial institution under the CPP.

§ 30.11 Q-11: How does section 111(b) of EESA operate in connection with an acquisition, merger, or reorganization?

(a) Special rules for acquisitions, mergers, or reorganizations. In the event that a financial institution (target) that had sold troubled assets to the Treasury through the CPP is acquired by an entity that is not related to target (acquirer) in an acquisition of any form, acquirer will not become subject to section 111(b) of EESA merely as a result of the acquisition. For this purpose, an acquirer is related to target if stock or other interests of target are treated (under 26 U.S.C. 318(a) other than paragraph (4) thereof) as owned by acquirer. With respect to the target, any employees of target who are SEOs prior to the acquisition will be subject to section 111(b)(2)(C) of EESA until after the first anniversary following the acquisition.

(b) Example. In 2008, financial institution A sells $100 million of troubled assets to the Treasury through the CPP. In January 2009, financial institution B, which is not otherwise subject to section 111(b) of EESA, acquires financial institution A in a stock purchase transaction, with the result that financial institution A becomes a wholly owned subsidiary of financial institution B. Based on the rules in paragraph (a) of this § 30.11 (Q-11), the SEOs of financial institution B are not subject to section 111(b) of EESA solely as a result of the acquisition of financial institution A in January 2009. The SEOs of financial institution A at the time of the acquisition are subject to section 111(b)(2)(C) of EESA until January 2010, the first anniversary following the acquisition.

Dated:____________

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Neel Kashkari
Interim Assistant Secretary for Financial Stability

Frequently Asked Questions (FAQs)
Executive Compensation Requirements under the Capital Purchase Program (CPP)

For what period do the executive compensation requirements set forth in 31 C.F.R. Part 30 promulgated under EESA section 111(b) (CPP executive compensation requirements) apply to the financial institution?

The executive compensation requirements apply to the financial institution for as long as Treasury holds any equity or debt position in the financial institution under the CPP, including the Warrant or any equity acquired under the Warrant.

How are senior executive officers (SEOs) identified for purposes of compliance with the CPP executive compensation requirements?

(a) Non-tax-related standards. For purposes of the non-tax-related executive compensation standards (no unnecessary and excessive risk taking, clawbacks of certain bonus or incentive compensation, and prohibition on golden parachute payments), the SEOs for a year are the "named executive officers" who are identified in the financial institution's annual report on Form 10-K or annual meeting proxy statement for that year (reporting the executive's compensation for the immediately preceding year). These executive officers are considered the SEOs throughout that entire year.

Prior to the identification of the named executive officers in the financial institution's annual report on Form 10-K or annual meeting proxy statement, the financial institution must make its best efforts to identify the year's SEOs for purposes of the applicability of the non-tax related executive compensation standards for the year. If any executive is a potential SEO and terminates employment in an involuntary termination prior to the identification of the year's named executive officers, the financial institution should refrain from making any golden parachute payment until the year's named executive officers are identified in either the annual report on Form 10-K or annual meeting proxy statement so that it can be determined whether the executive is a named executive officer and, therefore, is a SEO who is not entitled to the golden parachute payment for the year.

(b) Tax-related standard. The tax-related executive compensation standard requires financial institutions to agree not to claim a tax deduction for compensation paid to each SEO in an amount that exceeds $500,000. Because the contractual limitation on the amount of the tax deduction is based on current year compensation, the SEOs are determined based on compensation for that year, rather than compensation paid in the preceding year as described above. This means that for the purposes of the tax-related standard, SEOs are determined based on the financial institution's annual report on Form 10-K or annual meeting proxy statement for the year subsequent to the year in which the contractual limitation on the tax deduction applies.

(c) Private financial institutions. Rules analogous to those in paragraph (a) and (b) apply to financial institutions that do not have securities registered with the Securities and Exchange Commission (SEC) pursuant to the federal securities laws.

How must a financial institution that is defined as a "smaller reporting company " pursuant to Item 10 of Regulation S-K under the federal securities laws identify SEOs for purposes of compliance with the CPP executive compensation requirements?

A financial institution that is a "smaller reporting company" must identify SEOs pursuant to the rules set forth in section 30.2 of 31 C.F.R. Part 30 and the previous FAQ. Note that such a financial institution must identify at least five SEOs, even if only three SEOs are provided in the disclosure pursuant to section 402 of Regulation S-K under the federal securities laws.

How should a financial institution that is defined as a "smaller reporting company" pursuant to Item 10 of Regulation S-K under the federal securities laws provide the certifications of the compensation committee for purposes of compliance with the CPP executive compensation requirements?

A financial institution that is a "smaller reporting company" should provide the certifications of the compensation committee, or a committee acting in a similar capacity, to its primary regulatory agency.

To what primary regulatory agency should a state-chartered bank that does not have securities registered with the SEC pursuant to the federal securities laws provide the certifications of the compensation committee for purposes of compliance with the CPP executive compensation requirements?

In the case of a state-chartered bank that does not have securities registered with the SEC pursuant to the federal securities laws, the primary regulatory agency is its primary federal banking regulator.

For purposes of compliance with the CPP executive compensation requirements relating to the clawback provision, must a financial institution recover bonuses and incentive compensation based on financial statements that become materially inaccurate because of revisions to generally accepted accounting principles where the financial statements were accurate based on generally accepted accounting principles applicable when the payment was made?

No.

Are payments on account of involuntary termination of employment that are made after the period that the Treasury holds an equity or debt position under the CPP taken into account for purposes of the rules prohibiting golden parachute payments under the CPP executive compensation requirements?

Yes. A golden parachute payment is the aggregate present value of all payments made on account of an applicable severance of employment that equals or exceeds three times the

SEO's base amount. Thus, the determination of a golden parachute payment includes amounts paid during or after the period the Treasury holds an equity or debt position under the CPP. ([See § 1.280G-1, Q&A-38, of the Treasury Regulations for how to allocate the base amount to a series of payments made over multiple years.])

Please check back regularly for postings of additional Q&As.

H. R. 1424

One Hundred Tenth Congress of the United States of America

AT THE SECOND SESSION

Begun and held at the City of Washington on Thursday, the third day of January, two thousand and eight

An Act

To provide authority for the Federal Government to purchase and insure certain types of troubled assets for the purposes of providing stability to and preventing disruption in the economy and financial system and protecting taxpayers, to amend the Internal Revenue Code of 1986 to provide incentives for energy production and conservation, to extend certain expiring provisions, to provide individual income tax relief, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

DIVISION A—EMERGENCY ECONOMIC STABILIZATION

SECTION 1. SHORT TITLE AND TABLE OF CONTENTS.

(a) SHORT TITLE.—This division may be cited as the "Emergency Economic Stabilization Act of 2008".

SEC. 111. EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.

(a) APPLICABILITY.—Any financial institution that sells troubled assets to the Secretary under this Act shall be subject to the executive compensation requirements of subsections (b) and (c) and the provisions under the Internal Revenue Code of 1986, as provided under the amendment by section 302, as applicable.

(b) DIRECT PURCHASES.—

(1) IN GENERAL.—Where the Secretary determines that the purposes of this Act are best met through direct purchases of troubled assets from an individual financial institution where no bidding process or market prices are available, and the Secretary receives a meaningful equity or debt position in the financial institution as a result of the transaction, the Secretary shall require that the financial institution meet appropriate standards for executive compensation and corporate governance. The standards required under this subsection shall be effective for the duration of the period that the Secretary holds an equity or debt position in the financial institution.

(2) CRITERIA.—The standards required under this sub-section shall include—

(A) limits on compensation that exclude incentives for senior executive officers of a financial institution to take unnecessary and excessive risks that threaten the value of the financial institution during the period that the Secretary holds an equity or debt position in the financial institution;

(B) a provision for the recovery by the financial institution of any bonus or incentive compensation paid to a senior executive officer based on statements of earnings, gains, or other criteria that are later proven to be materially inaccurate; and

(C) a prohibition on the financial institution making any golden parachute payment to its senior executive officer during the period that the Secretary holds an equity or debt position in the financial institution.

(3) DEFINITION.—For purposes of this section, the term ''senior executive officer'' means an individual who is one of the top 5 highly paid executives of a public company, whose compensation is required to be disclosed pursuant to the Securities Exchange Act of 1934, and any regulations issued there-under, and non-public company counterparts.

(c) AUCTION PURCHASES.—Where the Secretary determines that the purposes of this Act are best met through auction purchases of troubled assets, and only where such purchases per financial institution in the aggregate exceed $300,000,000 (including direct purchases), the Secretary shall prohibit, for such financial institution, any new employment contract with a senior executive officer that provides a golden parachute in the event of an involuntary termination, bankruptcy filing, insolvency, or receivership. The Secretary shall issue guidance to carry out this paragraph not later than 2 months after the date of enactment of this Act, and such guidance shall be effective upon issuance.

(d) SUNSET.—The provisions of subsection (c) shall apply only to arrangements entered into during the period during which the authorities under section 101(a) are in effect, as determined under section 120.

SEC. 302. SPECIAL RULES FOR TAX TREATMENT OF EXECUTIVE COMPENSATION OF EMPLOYERS PARTICIPATING IN THE TROUBLED ASSETS RELIEF PROGRAM.

(a) DENIAL OF DEDUCTION.—Subsection (m) of section 162 of the Internal Revenue Code of 1986 is amended by adding at the end the following new paragraph:

''(5) SPECIAL RULE FOR APPLICATION TO EMPLOYERS PARTICI-PATING IN THE TROUBLED ASSETS RELIEF PROGRAM.—

''(A) IN GENERAL.—In the case of an applicable employer, no deduction shall be allowed under this chapter—

''(i) in the case of executive remuneration for any applicable taxable year which is attributable to services performed by a covered executive during such applicable taxable year, to the extent that the amount of such remuneration exceeds $500,000, or

''(ii) in the case of deferred deduction executive remuneration for any taxable year for services per-formed during any applicable taxable year by a covered executive, to the extent that the amount of such remuneration exceeds $500,000 reduced (but not below zero) by the sum of—

''(I) the executive remuneration for such applicable taxable year, plus

''(II) the portion of the deferred deduction executive remuneration for such services which was taken into account under this clause in a preceding taxable year.

''(B) APPLICABLE EMPLOYER.—For purposes of this paragraph—

''(i) IN GENERAL.—Except as provided in clause (ii), the term 'applicable employer' means any employer from whom 1 or more troubled assets are acquired under a program established by the Secretary under section 101(a) of the Emergency Economic Stabilization Act of 2008 if the aggregate amount of the assets so acquired for all taxable years exceeds $300,000,000.

''(ii) DISREGARD OF CERTAIN ASSETS SOLD THROUGH DIRECT PURCHASE.—If the only sales of troubled assets by an employer under the program described in clause (i) are through 1 or more direct purchases (within the meaning of section 113(c) of the Emergency Economic Stabilization Act of 2008), such assets shall not be taken into account under clause (i) in determining whether the employer is an applicable employer for purposes of this paragraph.

''(iii) AGGREGATION RULES.—Two or more persons who are treated as a single employer under subsection (b) or (c) of section 414 shall be treated as a single employer, except that in applying section 1563(a) for purposes of either such subsection, paragraphs (2) and (3) thereof shall be disregarded.

''(C) APPLICABLE TAXABLE YEAR.—For purposes of this paragraph, the term 'applicable taxable year' means, with respect to any employer—

''(i) the first taxable year of the employer—

''(I) which includes any portion of the period during which the authorities under section 101(a) of the Emergency Economic Stabilization Act of 2008 are in effect (determined under section 120 thereof), and

''(II) in which the aggregate amount of troubled assets acquired from the employer during the taxable year pursuant to such authorities (other than assets to which subparagraph (B)(ii) applies), when added to the aggregate amount so acquired for all preceding taxable years, exceeds $300,000,000, and

''(ii) any subsequent taxable year which includes any portion of such period.

''(D) COVERED EXECUTIVE.—For purposes of this paragraph—

''(i) IN GENERAL.—The term 'covered executive' means, with respect to any applicable taxable year, any employee—

''(I) who, at any time during the portion of the taxable year during which the authorities under section 101(a) of the Emergency Economic Stabilization Act of 2008 are in effect (determined under section 120 thereof), is the chief executive officer of the applicable employer or the chief financial officer of the applicable employer, or an individual acting in either such capacity, or

''(II) who is described in clause (ii).

''(ii) HIGHEST COMPENSATED EMPLOYEES.—An employee is described in this clause if the employee is 1 of the 3 highest compensated officers of the applicable employer for the taxable year (other than an individual described in clause (i)(I)), determined—

''(I) on the basis of the shareholder disclosure rules for compensation under the Securities Exchange Act of 1934 (without regard to whether those rules apply to the employer), and

''(II) by only taking into account employees employed during the portion of the taxable year described in clause (i)(I).

''(iii) EMPLOYEE REMAINS COVERED EXECUTIVE.— If an employee is a covered executive with respect to an applicable employer for any applicable taxable year, such employee shall be treated as a covered executive with respect to such employer for all subsequent applicable taxable years and for all subsequent taxable years in which deferred deduction executive remuneration with respect to services performed in all such applicable taxable years would (but for this paragraph) be deductible.

''(E) EXECUTIVE REMUNERATION.—For purposes of this paragraph, the term 'executive remuneration' means the applicable employee remuneration of the covered executive, as determined under paragraph (4) without regard to sub-paragraphs (B), (C), and (D) thereof. Such term shall not include any deferred deduction executive remuneration with respect to services performed in a prior applicable taxable year.

''(F) DEFERRED DEDUCTION EXECUTIVE REMUNERA-TION.—For purposes of this paragraph, the term 'deferred deduction executive remuneration' means remuneration which would be executive remuneration for services per-formed in an applicable taxable year but for the fact that the deduction under this chapter (determined without regard to this paragraph) for such remuneration is allow-able in a subsequent taxable year.

''(G) COORDINATION.—Rules similar to the rules of sub-paragraphs (F) and (G) of paragraph (4) shall apply for purposes of this paragraph.

''(H) REGULATORY AUTHORITY.—The Secretary may pre-scribe such guidance, rules, or regulations as are necessary to carry out the purposes of this paragraph and the Emergency Economic Stabilization Act of 2008, including the extent to which this paragraph applies in the case of any acquisition, merger, or reorganization of an applicable employer.''.

(b) GOLDEN PARACHUTE RULE.—Section 280G of the Internal Revenue Code of 1986 is amended—

(1) by redesignating subsection (e) as subsection (f), and

(2) by inserting after subsection (d) the following new sub-section:

''(e) SPECIAL RULE FOR APPLICATION TO EMPLOYERS PARTICI PATING IN THE TROUBLED ASSETS RELIEF PROGRAM.— -

'(1) IN GENERAL.—In the case of the severance from employment of a covered executive of an applicable employer during the period during which the authorities under section 101(a) of the Emergency Economic Stabilization Act of 2008 are in effect (determined under section 120 of such Act), this section shall be applied to payments to such executive with the following modifications:

''(A) Any reference to a disqualified individual (other than in subsection (c)) shall be treated as a reference to a covered executive.

''(B) Any reference to a change described in subsection (b)(2)(A)(i) shall be treated as a reference to an applicable severance from employment of a covered executive, and any reference to a payment contingent on such a change shall be treated as a reference to any payment made during an applicable taxable year of the employer on account of such applicable severance from employment.

''(C) Any reference to a corporation shall be treated as a reference to an applicable employer.

''(D) The provisions of subsections (b)(2)(C), (b)(4), (b)(5), and (d)(5) shall not apply.

''(2) DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection:

''(A) DEFINITIONS.—Any term used in this subsection which is also used in section 162(m)(5) shall have the meaning given such term by such section.

''(B) APPLICABLE SEVERANCE FROM EMPLOYMENT.—The term 'applicable severance from employment' means any severance from employment of a covered executive—

''(i) by reason of an involuntary termination of the executive by the employer, or ‘‘(ii) in connection with any bankruptcy, liquidation, or receivership of the employer.

‘‘(C) COORDINATION AND OTHER RULES.—

‘‘(i) IN GENERAL.—If a payment which is treated as a parachute payment by reason of this subsection is also a parachute payment determined without regard to this subsection, this subsection shall not apply to such payment.

‘‘(ii) REGULATORY AUTHORITY.—The Secretary may prescribe such guidance, rules, or regulations as are necessary—

‘‘(I) to carry out the purposes of this subsection and the Emergency Economic Stabilization Act of 2008, including the extent to which this subsection applies in the case of any acquisition, merger, or reorganization of an applicable employer,

‘‘(II) to apply this section and section 4999 in cases where one or more payments with respect to any individual are treated as parachute pay-ments by reason of this subsection, and other pay-ments with respect to such individual are treated as parachute payments under this section without regard to this subsection, and

‘‘(III) to prevent the avoidance of the applica-tion of this section through the mischaracterization of a severance from employment as other than an applicable severance from employment.’’.

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendment made by subsection (a) shall apply to taxable years ending on or after the date of the enactment of this Act.

(2) GOLDEN PARACHUTE RULE.—The amendments made by subsection (b) shall apply to payments with respect to severances occurring during the period during which the authorities under section 101(a) of this Act are in effect (deter-mined under section 120 of this Act).

(b) EXTENSION.—

(1) IN GENERAL.—Section 4611(f) (relating to application of Oil Spill Liability Trust Fund financing rate) is amended by striking paragraphs (2) and (3) and inserting the following new paragraph:

‘‘(2) TERMINATION.—The Oil Spill Liability Trust Fund financing rate shall not apply after December 31, 2017.’’.

(2) CONFORMING AMENDMENT.—Section 4611(f)(1) is amended by striking ‘‘paragraphs (2) and (3)’’ and inserting ‘‘paragraph (2)’’.

(3) EFFECTIVE DATE.—The amendments made by this sub-section shall take effect on the date of the enactment of this Act.

PRESS ROOM
U.S. DEPARTMENT OF THE TREASURY

February 4, 2009
TG-15

Treasury Announces New Restrictions On Executive Compensation

Today, the Treasury Department is issuing a new set of guidelines on executive pay for financial institutions that are receiving government assistance to address our current financial crisis. These measures are designed to ensure that public funds are directed only toward the public interest in strengthening our economy by stabilizing our financial system and not toward inappropriate private gain. The measures announced today are designed to ensure that the compensation of top executives in the financial community is closely aligned not only with the interests of shareholders and financial institutions, but with the taxpayers providing assistance to those companies.

The Treasury guidelines on executive pay seek to strike the correct balance between the need for strict monitoring and accountability on executive pay and the need for financial institutions to fully function and attract the talent pool that will maximize the chances of financial recovery and taxpayers being paid back on their investments. The proposals below, such as emphasizing restricted stock that vests as the government is repaid with interest, seek to strike exactly that balance.

The guidelines distinguish between banks participating in any new generally available capital access program and banks needing "exceptional assistance." Generally available programs have the same terms for all recipients, with limits on the amount each institution may receive and specified returns for taxpayers. The goal of these programs is to help ensure the financial system as a whole can provide the credit necessary for recovery, including providing capital to smaller community banks that play a critical role in lending to small businesses, families and others. The previously announced Capital Purchase Program is an example of a generally available capital access program.

If a firm needs more assistance than is allowed under a widely available standard program, then that is exceptional assistance. Banks falling under the "exceptional assistance" standard have bank-specific negotiated agreements with Treasury. Examples include AIG, and the Bank of America and Citi transactions under the Targeted Investment Program.

As part of President Obama's efforts to promote systemic regulatory reform, the standards today mark the beginning of a long-term effort to examine both the degree that executive compensation structures at financial institutions contributed to our current financial crisis and how corporate governance and compensation rules can be reformed to better promote long-term value and growth for shareholders, companies, workers and the economy at large and to prevent such financial crises from occurring again.

I. COMPLIANCE AND CERTIFICATION:

All Companies Receiving Government Assistance Must Ensure Compliance with Executive Compensation Provisions: The chief executive officers of all companies that have to this point received or do receive any form of government assistance must provide certification that the companies have strictly complied with statutory, Treasury, and contractual executive compensation restrictions. Chief executive officers must re-certify compliance with these restrictions on an annual basis. In addition, the compensation committees of all companies receiving government assistance must provide an explanation of how their senior executive compensation arrangements do not encourage excessive and unnecessary risk-taking.

II. ENHANCED CONDITIONS ON EXECUTIVE COMPENSATION

GOING FORWARD:

A. **Companies Receiving Exceptional Financial Recovery Assistance:**

- **Limit Senior Executives to $500,000 in Total Annual Compensation – Other than Restricted Stock:** Current programs providing exceptional assistance to financial institutions forbid recipients of government funds from taking a tax deduction for senior executive compensation above $500,000. Today's guidance takes this restriction further by limiting the total amount of compensation to no more than $500,000 for these senior executives except for restricted stock awards.
- **Any Additional Pay for Senior Executives Must Be in Restricted Stock that Vests When the Government Has Been Repaid with Interest:** Any pay to a senior executive of a company receiving exceptional assistance beyond $500,000 must be made in restricted stock or other similar long-term incentive arrangements. The senior executive receiving such restricted stock will only be able to cash in either after the government has been repaid – including the contractual dividend payments that ensure taxpayers are compensated for the time value of their money – or after a specified period according to conditions that consider among other factors the degree a company has satisfied repayment obligations, protected taxpayer interests or met lending and stability standards. Such a restricted stock strategy will help assure that senior executives of companies receiving exceptional assistance have incentives aligned with both the long-term interests of shareholders as well as minimizing the costs to taxpayers.
- **Executive Compensation Structure and Strategy Must be Fully Disclosed and Subject to a "Say on Pay" Shareholder Resolution:** The senior executive compensation structure and the rationale for how compensation is tied to sound risk management must be submitted to a non-binding shareholder resolution. There are no "Say on Pay" provisions in the existing programs.
- **Require Provisions to Clawback Bonuses for Top Executives Engaging in Deceptive Practices:** Under the existing programs providing exceptional assistance, only the top five senior executives were subject to a clawback provision. Going forward, a company receiving exceptional assistance must have in place provisions to claw back bonuses and incentive compensation from any of the next twenty senior executives if they are found to have knowingly engaged in providing inaccurate information relating to financial statements or performance metrics used to calculate their own incentive pay.
- **Increase Ban on Golden Parachutes for Senior Executives:** The existing programs providing exceptional assistance to financial institutions prohibited the top five senior executives from receiving any golden parachute payment upon severance from employment, a ban that will be expanded to include the top ten senior executives. In addition, and at a minimum, the next twenty-five executives will be prohibited from receiving any golden parachute payment greater than one year's compensation upon severance from employment.
- **Require Board of Directors' Adoption of Company Policy Relating to Approval of Luxury Expenditures:** The boards of directors of companies receiving exceptional assistance from the government must adopt a company-wide policy on any expenditures related to aviation services, office and facility renovations, entertainment and holiday parties, and conferences and events. This policy is not intended to cover reasonable expenditures for sales conferences, staff development, reasonable performance incentives and other measures tied to a company's normal business operations. These new rules go beyond current guidelines, and would require certification by chief executive officers for expenditures that could be viewed as excessive or luxury items. Companies should also now post the text of the expenditures policy on their web sites.

B. **Financial Institutions Participating in Generally Available Capital Access Programs:**

The Treasury intends to issue proposed guidance subject to public comment on the following executive compensation requirements relating to future *generally available* capital access programs.

- **Limit Senior Executives to $500,000 in Total Annual Compensation**

Plus Restricted Stock – U*n*less Waived with Full Public Disclosure and Shareholder Vote: Companies that participate in generally available capital access programs may waive the $500,000 plus restricted stock rule only by disclosure of their compensation and, if requested, a non-binding "say on pay" shareholder resolution. All firms participating in a future capital access program must review and disclose the reasons that compensation arrangements of both the senior executives and other employees do not encourage excessive and unnecessary risk taking. Under the current Capital Purchase Program, the companies were only required to review and certify that the top five executives' compensation arrangements did not encourage excessive and unnecessary risk-taking.

- **Require Provisions to Clawback Bonuses for Top Executives Engaging in Deceptive Practices:** The same clawback provision that applies to companies receiving exceptional assistance will apply to those in generally available capital access programs. Thus, in addition to the clawback provision applicable to the top five executives as under the Capital Purchase Program, a company receiving assistance must have in place provisions to claw back bonuses and incentive compensation from any of the next twenty senior executives if they are found to have knowingly engaged in providing inaccurate information relating to financial statements or performance metrics used to calculate their own incentive pay.
- **Increase Ban on Golden Parachutes for Senior Executives:** Even under generally available capital access programs, the golden parachute ban will be strengthened: Upon a severance from employment, the top five senior executives will not be allowed a golden parachute payment greater than one year's compensation, as opposed to three years under the current Capital Purchase Program.
- **Require Board of Directors' Adoption of Company Policy Relating to Approval of Luxury Expenditures:** This policy will be the same for companies accessing generally available capital programs as it is for those receiving exceptional assistance. There are no guidelines on luxury expenditures under the current Capital Purchase Program.

[*These new standards will not apply retroactively to existing investments or to programs already announced such as the Capital Purchase Program and the Term Asset-Backed Securities Loan Facility*.]

III. LONG-TERM REGULATORY REFORM: COMPENSATION STRATEGIES ALIGNED WITH PROPER RISK MANAGEMENT AND LONG-TERM VALUE AND GROWTH:

Even as we work to recover from current market events, it is not too early to begin a serious effort to both examine how company-wide compensation strategies at financial institutions – not just those related to top executives – may have encouraged excessive risk-taking that contributed to current market events and to begin developing model compensation policies for the future. Such steps should include:

- ***Requiring all Compensation Committees of Public Financial Institutions to Review and Disclose Strategies for Aligning Compensation with Sound Risk-Management:*** The Secretary of the Treasury and the Chairman of the Securities and Exchange Commission should work together to require compensation committees of all public financial institutions – not just those receiving government assistance – to review and disclose executive and certain employee compensation arrangements and explain how these compensation arrangements are consistent with promoting sound risk management and long-term value creation for their companies and their shareholders.
- C***ompensation of Top Executives Should Include Incentives That Encourage a Long-Term Perspective:*** Over the last decade there has been an emerging consensus that top executives should receive compensation that encourages more of a long-term perspective on creating economic value for their shareholders and the economy at large. One idea worthy of serious consideration is requiring top executives at financial institutions to hold stock for several years after it is awarded before it can be cashed-out as this would encourage a more long-term focus on the economic interests of the firm.
- ***Pass Say on Pay Shareholder Resolutions on Executive Compensation:*** Even beyond companies receiving financial recovery

assistance, owners of financial institutions – the shareholders – should have a non-binding resolution on both the levels of executive compensation as well as how the structure of compensation incentives help promote risk management and long-term value creation for the firm and the economy as a whole.

- ***White House -Treasury Conference on Long-Term Executive Pay Reform:*** The Secretary of the Treasury will host a conference with shareholder advocates, major public pension and institutional investor leaders, policy-makers, executives, academics, and others on executive pay reform at financial institutions. Treasury will seek testimony, comment, and white papers on model executive pay initiatives in the cause of establishing best practices and guidelines on executive compensation arrangements for financial institutions.

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