Business Roundtable

300 New Jersey Avenue, NW
Suite 800
Washington, DC 20001

Telephone 202.872.1260
Facsimile 202.466.3509
Website brt.org

July 20, 2016

The Honorable Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: File No. S7-07-16, Release No. 34-77776, IA-4383 Proposed Rule for Incentive-based Compensation Arrangements

Dear Secretary Fields:

This letter is submitted on behalf of Business Roundtable, an association of chief executive officers of leading U.S. companies. With $7 trillion in annual revenues and nearly 16 million employees, Business Roundtable companies comprise nearly one-fifth of the total value of the U.S. stock market.

We appreciate the opportunity to comment on the rule proposed by the U.S. Securities and Exchange Commission (SEC); the Office of the Comptroller of Currency, Department of Treasury; the Board of Governors of the Federal Reserve System; the Federal Deposit Insurance Corporation; the Federal Housing Finance Agency; and the National Credit Union Administration (together, the Agencies) pursuant to Section 956 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (*Dodd-Frank Act*), as set forth in the Agencies' proposing release on incentive-based compensation arrangements (proposed rule).

We are concerned that the proposed rule, in its current form, is overly prescriptive, could create additional tax compliance difficulties for the individuals and institutions to which it applies, and would make U.S. financial institutions less globally competitive. The proposed rule will also make it difficult for the institutions that pump capital through the U.S. and global economies to attract top talent. In addition, the proposed rule will create burdensome record keeping and corporate governance requirements.

Business Roundtable provides the following recommendations, which are intended to realize the goals of Section 956 of the *Dodd-Frank Act* while minimizing negative consequences for U.S. companies and the U.S. economy.

1. Definitions of Covered Persons and Significant Risk-Takers Should Be Narrowed

The definition of "covered persons," as outlined by the proposed rule, is overly broad and would cover the vast majority of employees in most covered institutions, as it encompasses employees that receive even a single dollar in incentive compensation.

The result is the population subject to the proposed rule would be excessively large, which expands the scope of oversight, governance and record keeping requirements for these employees. This approach would thus increase the scope of Section 956 of the *Dodd-Frank Act* and put multiple entities at a competitive disadvantage when it comes to talent recruitment and retention.

Thus we respectfully ask that the Agencies revise the meaning of covered persons to be limited to senior executive officers and significant risk-takers. This principles-based approach is currently employed in the 2010 Federal Banking Agency Guidance on Sound Incentive Compensation Policies, whereby the covered institution would have some flexibility to determine its covered persons, based on their risk profiles and the extent to which they could as individuals/groups expose the covered institution to material risk. This approach would be a more reasonable assessment of the population subject to the proposed rule.

We believe the test for determining significant risk-takers under the proposed rule will yield arbitrary results that are contrary to the stated intent of including employees in a "position to put a Level 1 or Level 2 covered institution at risk of material financial loss" (Federal Register, Vol. 81, No. 112, 6-2-16, page 37692). Because a factor in the test is the amount of compensation an employee receives rather than the employee's role, the test will, in some instances, exclude employees who could expose a financial institution to material financial loss and, in other instances, include employees who pose no risk to the institution. Because covered institutions may operate in multiple countries, utilize diverse technology systems, and have multiple incentive plans and many (often, thousands) of employees who receive incentive compensation, the proposed rule would impose a significant administrative burden while offering little in the way of compensating benefit.

The proposed rule's current definitions would result in a significant competitive disadvantage for covered institutions and make it hard to attract and retain top talent, especially those who are easily employable in other industries or smaller organizations, that may not be covered by the rule to the same extent.

2. Strike or Limit the Bright Line Minimum Deferral Requirements

The proposed rule imposes minimum bright line rules that require deferral of at least 40 percent to 60 percent of incentive compensation for senior executive officers and significant risk-takers at Level 1 and Level 2 covered institutions for at least three to four years – or for an additional one to two years after the end of a long-term incentive performance period.

These bright line deferral requirements leave Level 1 and Level 2 covered institutions with little flexibility to create incentive arrangements that reflect their business goals, compensation philosophies and cultures. The requirements will put Level 1 and Level 2 covered institutions at a significant disadvantage with respect to non-U.S. institutions in the global competition for top talent. They will remove the current competitive advantage U.S. institutions enjoy over their European counterparts that are already subject to similar requirements. Restricting the ability of U.S. financial institutions to attract the best talent will have a negative impact on the broader U.S. economy as well as on the institutions themselves.

Attempting to control systemic risk through compensation regulation is counterproductive. The proposed rule will stunt the ability of covered institutions to innovate, compete and grow. In effect, the proposed rule would sacrifice future innovation and economic growth in an attempt to limit potential risk. We think the negative economic consequences of the bright line deferral requirements significantly outweigh their potential to reduce systemic risk.

The bright line deferral requirement should be removed, and Level 1 and Level 2 covered institutions should be able to determine, within the spirit of the proposed rule, how to structure incentive arrangements in a way that appropriately balances risk and reward.

The proposed rule will surely spur additional consideration, internal discussion and action regarding risk management and compliance, without the need for minimum deferral rules.

If the bright line deferral requirements remain a part of the proposed rule, then we recommend that the deferral requirement apply only to awards granted under a long-term incentive plan or that the deferral requirement apply to annual bonuses on a reduced basis (in both proportion and duration).

Most employees – including those at Level 1 and Level 2 covered institutions – consider their annual bonuses as compensation that they can count on for purposes of their annual cash flow. These annual bonuses will almost certainly be considered "incentive-based compensation arrangements" under the proposed rule, subject to the minimum deferral requirements. Requiring that a significant portion of certain employees' annual bonuses be deferred for a fairly long time will essentially reduce pay for those employees. To counterbalance this effect, covered institutions may ultimately restructure their compensation packages to have greater base salaries and smaller annual bonuses, thereby reducing alignment between those employees and the covered institutions' performance.

Disallowing the payment of deferred incentive compensation on various termination scenarios may lead to employees feeling entrenched at their current employers, eroding the competitive environment that is our economy's strength. Ultimately, this could negatively impact each covered institution's performance and undermine U.S. economic growth.

To the extent the mandatory deferral requirement remains in place under the proposed rule, measures should be taken to recognize that those employees did, in fact, earn that money. Employees subject to the bright line deferral requirement should be able to borrow from the amounts they were forced to defer (despite other laws or regulations that might otherwise be considered to prohibit such loans). Also, any amounts that must be deferred under the proposed rule should be allowed to accelerate and be paid under certain circumstances, including if the employee is terminated without cause, quits for good reason or retires. If those amounts cannot be paid under those scenarios, large portions of an employee's compensation could be tied to the health and performance of a company at which he or she no longer works and/or has influence.

3. Structure Clawback Net of Taxes

Under the proposed rule, all incentive compensation awarded by Level 1 and Level 2 covered institutions to senior executive officers and significant risk-takers must be subject to recoupment, under certain circumstances, for at least seven years from the vesting date.

An employee who is required to repay compensation that was paid in a prior tax year faces complex tax consequences, because the Internal Revenue Service (IRS) generally disallows amending a prior year's tax return to exclude an amount that is later clawed back. There is no clear, consistent method under current income tax rules and procedures by which an employee could be reimbursed or made whole for amounts that were taxed in a prior year, but which must be paid back in their entirety in a later year. As a result, an employee who is required to repay incentive compensation could end up in a worse position than if they had never received the compensation in the first place.

To address this issue, if an employee must repay amounts under the proposed rule's clawback requirement, any such amounts should be limited to the actual amount received by the employee (i.e., less taxes that were withheld).

Given that clawback and recoupment policies are more prevalent, the IRS may develop clear procedures under which an employee who is required to pay back previously paid compensation can be put in a tax-neutral position despite such repayment. However, until that time, employees subject to the mandatory clawback period should be required to repay only the portion of the incentive compensation they actually received.

4. Reduce Excessive Written Reporting Requirements

To carry out effective governance practices under the proposed rule, boards or compensation committees of Level 1 and Level 2 covered institutions would, annually (or more frequently), obtain a written assessment of the covered institution's incentive compensation programs and related compliance and control processes from both the management team and the internal audit or risk management function.

Mandating the creation of two sets of internal assessments no less frequently than on an annual basis is not only a costly administrative burden – it may also have the unintended consequence of making it more difficult to have a thoughtful and meaningful review of the institution's incentive compensation plans and processes. An annual review process does not allow an incentive cycle to play out or the chance to take a step back and evaluate the effectiveness of the incentive programs and processes. The governance requirement will become a compliance exercise, rather than an effective process to foster sound risk management.

The additional mandated governance requirements that apply to Level 1 and Level 2 covered institutions should be removed, giving each such institution the flexibility to create a review process that fits within its existing governance framework and that is considered by the institution's governance team as an efficient way to monitor compliance with the proposed rule.

If the additional requirement is not removed, both the written assessment requirement should be removed and the frequency with which the mandated review be completed should be extended to every three years, rather than on an annual basis.

Removing the written report requirement would foster a more fluid, honest assessment of potential risks. It will also be more efficient and less administratively burdensome. A covered institution will, of course, have the option to create written reports, if that suits the institution's processes and culture and what is ultimately determined by the board or compensation committee to be the most effective means to accomplish this particular oversight and assessment function. However, those institutions for which written reports would not foster the most effective governance system would not be required to fit a certain mold.

Allowing the assessments to occur on a less frequent basis than annually would enable an institution to determine the frequency that it deems most appropriate. We recommend required assessments occur no more often than three years – coinciding with the relatively common three-year long-term incentive performance cycle. An institution would, therefore, have the chance to allow for a full long-term incentive cycle and then review the incentive plans and programs as a whole (taking into account both short-term incentives and long-term incentives). Not only would it allow for a more meaningful review, but it would also be less expensive for shareholders.

Thank you for considering our comments and recommendations. We would be happy to discuss our concerns or any other matters that you believe would be helpful. Please contact Maria Ghazal, General Counsel of Business Roundtable, at [redacted] or [redacted].

Sincerely,

John Hayes
Chairman, President and Chief Executive Officer
Ball Corporation
Chair, Corporate Governance Committee
Business Roundtable

CC: The Office of the Comptroller of Currency, Department of Treasury
The Board of Governors of the Federal Reserve System
The Federal Deposit Insurance Corporation
The Federal Housing Finance Agency
The National Credit Union Administration