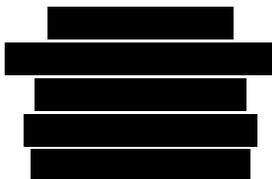


Seymour Smidt



May 27, 2011

Re: File Number S7-12-11

Comment on Proposed Incentive-Based Compensation Rules

Getting it Right

It is hard to exaggerate the importance of getting these rules right. Excessive risk-taking was the main reason that so many large financial institutions failed during the Great Recession. And many more institutions (some would say nearly all) would have failed if not for vigorous government intervention. As President Obama recently said, “As everybody here knows.....this was probably the most unpopular thing that -- government has maybe ever done -- was helping banks who helped cause the crisis.”¹ Because it was so unpopular the rules have changed: if a crisis of similar magnitude were to occur again under current legislation, the kind of bailouts used last time would be illegal.²

No one can possibly know in advance exactly what getting it right means. If one considers the costs to society of having rules so strict that there is too little risk-taking, versus the cost of rules that are so permissive that there is too much risk-taking, I believe that we need to err on the side of too little risk-taking. The widespread use of derivatives makes it harder (I suspect practically impossible) to judge how much risk is embedded in the system by looking at the balance sheets of financial institutions (think AIG). Therefore, traditional methods of controlling risk by imposing capital controls are ineffective.

Working on motivations is a more promising approach. To put it crudely, greed motivates people to take greater risks, because risky investments have higher expected payoffs. Similarly, fear of losses motivates people to take fewer risks. The amount of risk in the system reflects a balance between greed and fear, between the desire for higher returns and the fear of losses. To decrease the amount of risk in the system, we need to increase the size of the losses that decision makers incur when things go badly. Section 956 is a mandate to reduce inappropriate risk-taking in financial institutions. The recommendations in this comment are designed to make the proposed rules more effective in achieving that goal.

¹ (Obama, Hill, and Smith)

² See Dodd Frank Law, Title II, Orderly Liquidation Authority, especially Section 214 (a), which states in part that “no taxpayer funds shall be used to prevent the liquidation of any financial company under this title.”

Compensation Arrangements: Incentive-based and Others

It is important to recognize that there may be strong incentives for performance that have nothing to do with compensation. In many occupations highly motivated people commit great effort, and in some cases expose themselves to personal harm to achieve goals they believe are important even though their compensation arrangements have no incentive component. The President of the United States, members of Congress, the commissioned and noncommissioned members of the armed forces, police officers and firefighters, members of the Foreign Service, most professional athletes and almost all amateur athletes are examples.

Excellent performance may be and frequently is rewarded with additional compensation even when there is no incentive-based compensation system in place. The possibilities of future promotions and/or merit pay increases acknowledge and encourage excellent performance but do not, in themselves, constitute an incentive-based compensation system.

In some positions, not all of the important aspects of performance are equally measurable. In such cases introducing performance pay for the measurable aspects can lead to distortions in efforts that degrade the overall performance. The debate over performance based pay for public school teachers illustrates the complexity of the problem.

Incentive-based Compensation (IBC) and Investment Risk

Characterizing an investment as risky implies more than just some uncertainty about the outcomes. If there is no possibility of loss, there is no risk. In a risky investment, not only is there uncertainty about the outcomes, but there are some possible outcomes (losses) that make the investment's owners worse off as well as other outcomes (gains) that make the owners better off than without the investment.

An IBC system that provides additional compensation as a reward when a recommended investment produces gains should also provide penalties when that investment produces losses. If an IBC system provides only rewards for recommenders of a risky investment, but no penalties, then the investment would be risky for its owners but not for the decision-makers who recommended it.

The definition of compensation in the proposed rule seems to include only rewards.

Recommendation A: Compensation should be defined as the totality of the financial relationships between the employer and the employee including both rewards and penalties.

Permitting incentive-based compensation systems that contain rewards but do not contain penalties will encourage employees to recommend risky investments without considering the losses they impose on the owners. An IBC system that does not penalize recommenders when bad outcomes occur will almost certainly result in positive recommendations for inappropriately risky investments.

Recommendation B: Incentive-based compensation arrangements must include both rewards and penalties. Incentive-based compensation systems that include rewards, but do not include penalties should be prohibited.

Measuring Gains and Losses

Finance theory teaches us that in evaluating investments, we can't just compare the expected rates of return.³ If investment A has an expected return of 8% and investment B has an expected return of 12%, B is not necessarily a better investment than A. We need to measure each investment's risk, and the returns that are typically available in the market for investments with that degree of risk.

Suppose the risk measure for investment A is 4% and that investments with a 4% risk measure are priced in the market to produce a 6% expected rate of return. It is common to refer to 6% as the required rate of return for investment A. Under these conditions A is a desirable investment because its 8% expected rate of return is greater than its 6% required rate of return. The rewards and penalties associated with A need to be measured relative to its required rate of return. If A actually earns 11% in a given year, the reward to the decision maker should be scaled to reflect the fact that A's return was 5% above the required level. If in another year the actual return for A was 4%, then the penalty for the decision-maker should be scaled to reflect the fact that the actual return was 2% less than the required return.

Similarly, suppose the risk measure for B is 12% and that 14% is the required rate of return for investments with a 12% risk measure. Then B is an undesirable investment because its 12% expected rate of return is less than its required 14% rate of return. If B were actually accepted, the rewards and penalties associated with B would need to be measured relative to its required rate of return. If B actually earns 8% in a given year, the penalty to the decision maker should be scaled to reflect the fact that B's return was 6% below the required level. If the actual return for B was 20%, then the reward for the decision-maker should be scaled to reflect the fact that the actual return was 6% more than the required return.

Recommendation C: In any incentive-based compensation system, the incentive rewards and penalties should be measured relative to the required returns of the investment and not relative to zero.

To the extent possible, appropriate risk-management, risk-oversight and/or internal control personnel should be involved in determining the required rates of return of investments.

Balance of Risk and Rewards

An important difficulty in designing an acceptable IBC system is that most employees have a much more limited ability to absorb losses than the organizations for which they work. The following recommendation is designed to mitigate that problem by deferring payments of rewards to create an asset against which penalties may be charged. In circumstances in which it is not practical to include appropriate losses in an IBC system, the IBC system should not be used.

Recommendation D: A deferred compensation account (DCA) should be established for each person who participates in an IBC arrangement. Rewards from all of that person's activities should be deposited to that account and all penalties should be charged to that account. No payments should be

³ Think of the expected rate of return as the expected gain per dollar invested.

made from the account to the person until the positive balance in the account is larger than the maximum total penalties (MTP) that might be charged to the account under a worst case scenario for the firm and the economy.

There are many financial investments that have a high probability of a small gain and a small; probability of a large loss. One example is shorting deep out-of-the-money call options that have a short time to maturity. Suppose a trader is considering a strategy of taking short positions in certain call options provided that the exercise price is 25% greater than the price of the underlying stock and that the option has one month or less until it expires. Nearly all of the time, such trades will produce a small profit. But on rare occasions an underlying stock might double its price in less than a month producing a large loss. Under recommendation D, there is no need to decide if each transaction is considered to be a separate investment, on which a reward is paid when that particular option expires. Every time a short position is opened, the MTP for the trader's DCA should be increased accordingly.

A positive balance in a DCA is a contingent liability from the point of view of the firm. Just as the firm pays dividends to stockholders and interest to debtors, it should expect to pay an appropriate return on this contingent liability. The details on this topic require further study.

Generally, giving an employee greater responsibility for incentive-based activities should result in an increase in the MTP associated with his DCA. If the incentive-based compensation system is doing its job, the size of an individual's DCA could be considerable. As a guesstimate, for upper middle managers, amounts on the order of \$50 million should not be uncommon.

In case of bankruptcy, the balances owed on DCA accounts should be subordinate to any other debt, and to any preferred stock. The total value of all the DCA accounts at an investment bank once the system is operating in a stable equilibrium might be on the same order of magnitude as the book value of equity at the bank. This is a new kind of security that should add considerably to the bank's financial stability. In good times, the value of the liabilities should grow as new incentive awards are added to the accounts. In bad times the value of the liabilities should decline as penalties from disappointing investments reduce the total value of the DCA accounts.

From Partnerships to Corporations

Some background on how the partnership system worked will be helpful because although investment banks are no longer partnerships, many traditions that developed during the partnership era have been carried over to the era of corporations.

Until 1970 the rules of the New York Stock Exchange (NYSE) required all member firms to be partnerships. While not all NYSE member firms were investment banks, all important investment banks were NYSE members, and were therefore required to be partnerships.

In 1969 Donaldson, Lufkin & Jenrette, a young but very successful firm that specialized in serving institutions, decided that it needed more capital to grow and that the best way to get it was to incorporate and sell stock to the public. It informed the NYSE that it was going public the next year, and

that if necessary, it would resign from the NYSE in order to do that. The NYSE, with SEC approval, changed its rules and allowed member firms to become publically traded corporations. In the next couple of years, First Boston, Merrill Lynch, Dean Witter and E. F. Hutton went public. There was another wave of public offerings in the mid 1980's, including Bear Stearns in 1985 and Morgan Stanley the next year. The last major holdout, Goldman Sachs, went public in 1999.

In a partnership, each general partner is an owner of the business, contributes some of the capital, is authorized to act on behalf of the partnership and is personally responsible for all of its debts. Taking someone into a partnership is not too different from giving him or her power of attorney to dispose of the partnership's assets. It is not something that is taken lightly. When Goldman Sachs was still a partnership, one of their recruiters told me that the firm interviewed an average of 300 people for each entry level position that it filled.

In the partnership era a person who was recruited as an executive at an investment bank began as an associate. He was trained and given various assignments. After 6, 8 or 10 years of successful accomplishment at increasingly more responsible positions the best associates might be offered the opportunity to become partners. That was a major career milestone. The newly selected partners had to purchase a share in the partnership. Of course most of the young men (there were no women partners in those days) who had been selected did not have the wherewithal to buy a share in a successful investment banking partnership. So the partnership lent them the money needed to buy their partnership shares. A large part of their share of the partnership's earnings was deducted to pay the interest and principal on the loan. Although partners might be earning large incomes, they did not have large amounts of disposable cash. When partners retired, their ownership positions were converted to loans that were gradually paid out to over a five or ten year period. The result was that the partners of a successful investment bank did not have huge amounts of disposable liquid assets until sometime after their careers were over. The active partners typically had a large share of their personal wealth tied up in the partnership. Since they were personally liable for the firm's debts, they had a strong incentive to minimize risks.

The revenues of the investment banks in those days were subject to extreme and unpredictable year-to-year variation. To cope with their revenue volatility, the firms needed very low fixed costs. To achieve these low costs, investment banking partnerships developed a two-part compensation system that they applied not only to partners but to nearly all employees, including clerical staff. One part consisted of a guaranteed weekly or monthly salary. The second part consisted of an end-of-year lump sum payment whose size depended on how much the firm earned that year. This end-of-year lump sum, which was really a profit sharing distribution, is commonly but misleadingly referred to as a bonus. The guaranteed periodic salary component was less than the normal compensation for that position. When the expected bonus was taken into account the expected total compensation was above the normal level. "In 1993 first year partners [in Goldman Sachs] had 0.25 percent of the firm's more than \$2.6 billion in

pre-tax profits, or about \$6.5 million, contributed to their capital accounts.”⁴ Goldman Sachs was still a partnership at that time.

When the investment banking firms went public, the “bonus” system was still used to determine how much compensation should be paid. The large independent investment banks allocated about 50% of their top line (revenues minus interest expense) to employee compensation. That percentage remained remarkably steady from year to year; so variations in revenue were reflected directly in variations in compensation, just as if the firm were still a partnership. The balance of the top line went to pay other expenses and what was left went to stockholders. What changed dramatically when the investment banks converted to publically held corporations was the investment policy. As partnerships, they were very conservative, since the money at risk was their own. When they converted to public corporations, the incentive to minimize investment risk no longer existed to the same extent since most of the money at risk belonged to the stockholders, not the investment bankers and traders who were making the decisions.

During the housing boom investment banks became so highly leveraged that nearly any negative surprise would have caused them to fail. The factors of greed and fear were still at work, but the circumstances had changed. The decision makers still benefited if a risky decision turned out well. But if it turned out badly, most of the losses were absorbed by stockholders. To reduce excessive risk-taking, the system needs to be changed so that the decision makers bear a more appropriate share of the losses when decisions go wrong. (See recommendation E, below.)

A Hypothetical Example

People complain that generals are always devising strategies to fight the last war. I sympathize with the generals, because it is so hard to know what the next war will be like. But the generals have no excuse if the strategies they devise aren’t even adequate to win the last war. Devising strategies to prevent the next financial crisis presents similar problems.

As a reality check to see whether the incentive compensation rules proposed in response to section 956 of the Dodd-Frank Act are on the right track, I present a description of a hypothetical investment bank as it was operating in 2006, before the incentive-based compensation rules were adopted. The question to be considered is: What changes, if any, would have been required if this hypothetical bank had been required to comply with the proposed IBC rules?

For convenience I will refer to this fictional hypothetical investment bank as Bare Sterns. The name may sound like that of a real bank, because all fiction is ultimately inspired by reality, but please do not confuse this hypothetical bank with any real bank. Concentrate on the hypothetical bank and be careful not to attribute to it any unspecified characteristics of the real bank whose name has a similar sound.

Description: At Bare Sterns, a Performance Compensation Plan administered by the compensation committee of the Board of Directors was applicable to the company’s five executive officers and its 680

⁴ (Wilhelm and Downing 2001). p. 132.

managing directors. Each of these persons received compensation consisting of an annual salary, which was \$250,000 in 2006, plus shares in one or more bonus pools. One bonus pool was the source for the executive committee members' bonuses and other bonus pools were the sources of funds for the bonuses of groups of managing directors. Near the beginning of each year, the compensation committee adopted a formula to determine the size of each bonus pool. For many years, up to and including 2006, the performance measure that the Board of Directors chose to determine the size of the executive committee bonus pool was the after-tax return on the average equity (ROE).⁵

The main components of the performance based compensation for each person were cash, restricted stock and stock options. Nearly half of the performance based compensation was paid in the form of cash, which had no restrictions or provisions for clawback. Fifty percent of the restricted stock vested at the end of the second year and 50% at the end of the third year. But the stock could not be transferred until the end of the fifth year. The options had an exercise price equal to the market price of Bare Stern's stock on the day of the grant. They had a life of 10 years and were exercisable after 3 years.

If Bare Sterns had operated with no debt in 2006, its ROE would have equaled its after-tax return on assets (ROA), which was 1.95%. An ROA of 1.95% is nothing to get excited about. Few if any non-financial companies could survive if their ROA were that low. There are surely many pushcart hot-dog vendors on the sidewalks of Wall Street whose ROAs are much higher. With the same low ROA and 50% debt, the ROE would have been 2.5%. With 90% debt it would have been 6.8%. In fact, the Bare Stern executives were able to operate using 96.5% debt and only 3.5% equity, which produced a ROE of 17%. Reducing the proportion of equity to 3.5% of assets is actually quite an achievement. A non-financial company probably could not operate with such a small proportion of equity. Bare Sterns was able to do so because nearly all of its assets are marketable securities that can be given to lenders as collateral to secure short term loans. With that kind of collateral, lenders tend to worry less about the financial condition of the borrower. Another consideration was that the overwhelming majority of Bare Sterns' debt was very short term. Much of the money was borrowed for just 24 hours at a time and routinely renewed. Under these conditions a lender who became just the slightest bit nervous about the safety of the loan, for whatever reason, could just fail to renew. This was a great comfort to the lenders. It should have been a source of great discomfort to Bare Sterns, because it meant that their ability to borrow the amounts they needed could disappear on short notice.

The 17% ROE translated into a bonus pool of \$140 million for the executive committee, an average of \$28 million per person. The bonus pool was a little larger than usual in 2006, but only a little. During the five years ending in 2006, three of the members of the executive committee each received total cash compensation exceeding \$55 million dollars.

Bare Sterns was a large financial institution, with total assets of \$350 billion, operating with only \$12 billion of equity. A 3.5% decline in the value of its assets would wipe out its equity.

⁵ The after-tax return on average equity equals the after-tax income available to common stockholders divided by the average of the book values of the equity at the beginning and end of the year. From here on, ROE is used to refer to this measure.

Interpretation: Two facts about ROE should be well known to any student who passed even one course in corporate finance. The first is that if the return on assets is greater than the cost of debt, the ROE will increase as the amount of equity is reduced by substituting debt for equity. The second is that if the amount of equity is reduced by substituting debt for equity, the remaining equity will become more risky. For example, suppose there is an unexpected one percent decline in the value of an institution's assets: If the institution had a debt to asset ratio of 50%, the value of its equity would decline by 2 %. If its debt to asset ratio were 96.5%, the value of its equity would decline by 30%.

The executives of Bare Sterns took a pretty mediocre ROA and converted it to a rather interesting ROE entirely by using a high proportion of debt and very little equity. That strategy imposed substantial risk on the institution's stockholders. The compensation committee of the Bare Sterns Board of Directors did not explain why it chose ROE as the performance measure that it used to determine the size of the executive committee bonus pool. Operating a large financial institution so as to maximize its ROE is the financial equivalent of driving a powerful sports car on a crowded freeway with the pedal on the metal. Both situations are examples of an accident waiting to happen. At least in the case of the sports car, the driver would be violating the speed limit.

Do the incentive compensation practices being used by Bare Sterns violate any of the proposed rules as published? I am afraid they don't. The deferral arrangements in this hypothetical situation might not have met the exact requirements of the deferral rules proposed for executive officers in large covered financial institutions in the proposed rule, but in some respects they were more stringent. Certainly they could have been made to comply with no great trouble and with no material change in the incentives of the executive officers.

If the recommendations previously suggested in this note were included in the final version of the rules, then the incentive compensation practices being used by Bare Sterns would not comply. Specifically, this incentive compensation system violates recommendation B in that there are rewards but no penalties.

Compensation of Executive Officers

Two statements in the Background section of the Federal Register notice of the proposed rule on Incentive-based Compensation Arrangements are particularly worth noting on this topic.

"The Agencies believe that flawed incentive compensation practices in the financial industry were one of many factors contributing to the financial crisis that began in 2007."

"Managers and employees of a covered financial institution may be willing to tolerate a degree of risk that is inconsistent with broader public policy goals."

I strongly agree with these statements. The high degree of risk-taking that was pervasive among large financial institutions before the Great Recession was excessive from a public policy perspective and probably from the point of view of the shareholders of these institutions.

It is important to understand that, although the high degree of risk-taking referred to above was excessive from the point of view of stockholders, it was not excessive from the point of view of many of

the control executives of the institutions that failed. Most of those control executives were extremely rich before the financial meltdown and they are still very rich after the meltdown. I used the term rich to refer to persons who control sufficient financial resources so that there are no meaningful financial constraints preventing the persons from doing what they want (unless of course what they want is to be even richer than they are).

Being rich does not mean that you can have whatever you want. A rich person may want to be beautiful, happy, loved, famous, brilliant, accomplished, healthy, an admired celebrity, a world-class bridge player or whatever and be frustrated in some or all of these desires. Being rich just means that a lack of money is not preventing you from achieving your desires.

If you are not rich, then spending more on one thing means that you must spend less on something else. This is called a budget constraint. The theory of the consumer in standard economic theory is built on the assumption that the consumer is subject to a budget constraint. Such a person is not rich. The standard thinking about how to motivate business executives to align their interests with those of their stockholders is built on the assumption that they are not rich. It is not very relevant to many executives in today's world.

How much money does a person need in order to be rich? There is no simple answer to that question. But as a practical matter, I think it is safe to assume that a family whose net worth is \$50 million or more will behave as if they are rich. Many whose net worth is a much less than \$50 million will also.

There are probably many control executives in large financial institutions who are rich. By itself, being rich is not a problem. The problem arises if they are able to arrange their affairs so that they will continue to be rich whatever happens to the organizations that they control. In that case they are immune from financial incentives that organizations use to motivate their executives. If there are financial incentives that encourage them to go in a certain direction they might go in that direction because that is the direction they wanted to go anyway. But if they chose to go in a different direction the lack of financial incentives to support their chosen path is of no great consequence to them.

From a private point of view it is wonderful to be rich and it is perfectly understandable why so many people focus on attaining that goal as a major objective in their lives. But from a public policy point of view it is really scary to have rich people in the role of control executives in large covered financial institutions. They can do a lot of damage to the rest of us without hurting themselves financially. To change this situation, some financial incentives need to be created that will attract their attention. These new incentives must ensure that if their organization gets into trouble, they will no longer be rich.⁶

There are at least a few well respected and experienced observers of the American financial sector who support this idea, as indicated by the following quotations.

⁶ By this standard, the suggested deferral arrangements for executive officers of larger covered financial institutions are demonstrably inadequate. Some of the large financial institutions that failed during the recession had more stringent required deferral periods.

An interesting speculation is whether the crisis that emerged in August, 2007 from the extraordinary leverage (as much as 20 to 30 times tangible capital) taken on by the American investment banks almost surely would not have occurred had these firms remained the partnerships they were up to a quarter century ago.Prior to incorporation, those entities fearful of the joint and several liability of general partnerships shied away from virtually any risk they could avoid....

To be sure the senior officers of Bear Stearns and Lehman Brothers lost hundreds of millions of dollars from the collapse of their stocks. But none to my knowledge filed for personal bankruptcy and their remaining wealth allowed them to maintain much of their previous standards of living. Replicating the incentive structure of partnerships should be a goal whenever feasible in future reform.⁷

Alan Greenspan, The Crisis, March 10, 2010

if I was running things, if a bank had to go to the government for help, the CEO and his wife would forfeit all their net worth. And that would apply to any CEO that had been there in the previous two years..... It is nice to have carrots, but you need sticks. – the idea that some guy who's worth \$500 million leaves and only has \$50 million left is not much of a stick as far as I am concerned..... I really think there ought to be huge downsides because the CEO has to be the chief risk officer of a big bank..... make it so the CEO of the institution that fails or that goes with the government and needs help really gets destroyed himself financially.⁸

Warren Buffett, Fox Business News Network Interview, January 21, 2010

I think the insights in these quotations are right on target. William D. Cohan has made a similar suggestion.⁹ Neither of the gentlemen quoted formulated their insights into an operational form. I make an effort in that direction. The experts in the various agencies can surely improve my proposal if they agree with the objective. If the following recommendation seems Draconian, re-read the first section of this comment and reconsider.

There are a number of difficult issues. One has to do with coverage. It should of course include the CEO. But really large institutions are not run by just one person, and we have the example of Enron in which the CFO misled the Board of Directors and probably his fellow officers about the extent to which he was actually implementing Board policies designed to limit conflicts of interest and excessive risk-taking. The inspiration for the policy is the partnership model; going this route would suggest broadening the control group to include all covered persons.

If a person subject to unlimited liability could shed that responsibility when future trouble was expected, a large part of the benefits would be lost. I think that the exposure of a person who was subject to unlimited liability should continue for at least five years after the person had ended any active role in the organization and any affiliated organization. In the sixth year, liability should be limited to 80% of the subject person's personal assets. In each subsequent year liability would drop by another 20%. In the event of a subject person's death by accident or natural causes, the liability would drop to 50% of what it would have been if living. The death benefit should not apply if the death was self-inflicted or due to the person's reckless behavior (DUI, etc.).

⁷ (Greenspan 2010, 1-1-66), p 33.

⁸ (Buffet and Claman 2010)

⁹ (Cohan 2010)

Recommendation E: Once a person becomes an executive officer of a covered financial institution, that person shall have unlimited personal liability for the debts of the institution and its subsidiaries for as long as the person continues an active role in the affairs of the institution, plus the next five additional years. In the following four years, personal liability will be limited to 80%, 60%, 40% and 20% respectively. In the event of subject person’s death by accident or natural causes, the liability would drop to 50% of what it would have been if living.

An alternative version of recommendation E would substitute “a covered person” for “an executive officer.”

Financial Theory and Section 956(b)

Section 956 (b) includes the following passage:

“regulators shall prescribe regulations or guidelines that prohibit any types of incentive-based payment arrangement, or any feature of any such arrangement, that the regulators determine encourages inappropriate risks by covered financial institutions—

- (1) by providing an executive officer, employee, director, or principal shareholder of the covered financial institution with excessive compensation, fees, or benefits; or
- (2) that could lead to material financial loss to the covered financial institution.

In thinking about this section I found it helpful to define certain phrases in terms that could be related to standard financial theory. I think of inappropriate risks as occurring when the expected return of an investment is less than its required return, or more generally when the value of the risks imposed by an action are greater than its expected benefits. In the context of an IBC system excessive compensation occurs if the IBC tends to encourage accepting investments that have inappropriate risks. An example would be an IBC that produces rewards when good events occur but only minor penalties or none at all when bad events occur. I also found it useful to think of a material financial loss to a covered financial institution as a loss whose occurrence required extraordinary government intervention to control the resulting systemic risk.

Use of Plain Language

The Federal Registrar entry on Incentive-based Compensation Arrangements was very well organized and almost all of it was written in a clear understandable style. The only exception I encountered was the small section on “Risk Adjustment of Rewards.” I found that section completely incomprehensible. Perhaps an example would have helped.

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