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May 31, 2011

Via Electronic Delivery

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Washington, DC 20219

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System ("Federal Reserve")
20th Street and Constitution Avenue, NW
Washington, DC 20551

Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation ("FDIC")
550 17th Street, NW
Washington, DC 20429

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision ("OTS")
1700 G Street, NW
Washington, DC 20552

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission ("SEC")
100 F Street, NE
Washington, DC 20549

Re: Proposed Rules on Incentive-Based Compensation Arrangements (OCC Docket ID OCC-2011-0001; Federal Reserve Docket No. R-1410 and RIN No. 7100-AD69; FDIC RIN No. 3064-AD56; OTS Docket No. OTS-2011-0004; SEC File Number S7-12-11)

Gentleman and Ladies:

Pursuant to Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), the OCC, the Federal Reserve, the FDIC, the OTS, the National

Credit Union Administration, the SEC and the Federal Housing Finance Agency (collectively, the "Regulators") have jointly issued substantially identical proposed rules on incentive-based compensation arrangements (the "Proposed Rules"). The Securities Industry and Financial Markets Association ("SIFMA")[1] submits this letter to the Regulators listed above, each of whom serves as the "appropriate Federal regulator" (as defined in the Proposed Rules) for one or more SIFMA members, in response to the Regulators' request for comments regarding the Proposed Rules. Although we support ensuring that incentive-based compensation arrangements are consistent with overall safety and soundness, we believe that a number of important clarifications and modifications are necessary in order to ensure that the Proposed Rules appropriately address this goal. In particular, we believe that dictating the form of compensation that must be paid to executive officers is neither required by the Dodd-Frank Act nor an appropriate policy response to address the risks raised by improper incentives.

As a threshold matter, we note that pursuant to Executive Order 13563 (the "Executive Order"), entitled "Improving Regulation and Regulatory Review" and issued by President Obama on January 18, 2011, Federal regulators are urged to create a regulatory process that "protect[s] public health, welfare, safety, and our environment while promoting economic growth, innovation, competitiveness, and job creation." The Executive Order encourages regulators to "take into account benefits and costs" and "use the…least burdensome tools for achieving regulatory ends" in creating new regulations. We urge the Regulators to consider the Executive Order in their assessment of the Proposed Rules and whether they achieve the goals of Section 956 of the Dodd Frank Act in an efficient and appropriate manner. In particular, as described in more detail below, we believe that:

- The Proposed Rules' application to controlled groups with more than one covered financial institution should be clarified to ensure that the coverage of the Proposed Rules is appropriately tailored to achieve the purpose of the Dodd-Frank Act and that a lead regulator is appointed for the controlled group to avoid the potential for duplicative reports being filed with multiple regulators and inconsistent and overlapping interpretations of the rules.

- The prescriptive rule for deferral of compensation of executive officers is not the least burdensome method to achieve the regulatory goals and is not mandated by Section 956.

- The requirement to report the incentive compensation arrangements for <u>each</u> employee is needlessly burdensome.

- The definition of executive officer and other concepts in the Proposed Rules should be harmonized with existing regulations issued by many of the Regulators designed to address the same policy issues as the Proposed Rules are designed to address.

[1] The Securities Industry and Financial Markets Association (SIFMA) brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

1. Application of Proposed Rules to Controlled Groups

The Regulators should clarify how the Proposed Rules apply to covered financial institutions that are part of a larger controlled group that contains more than one entity that is a covered financial institution. For example, a bank holding company may have both a broker dealer subsidiary and an investment adviser subsidiary, with all three entities meeting the $1 billion threshold to be considered a covered financial institution under the Proposed Rules. We suggest that:

- To ensure consistent regulation, the controlled group should have one primary regulator that is responsible for overseeing the covered financial institutions within the group. Compensation systems are frequently designed at the holding company and implemented at each subsidiary (as well as at the holding company). If different entities within a controlled group were subject to oversight by different Regulators, the results could be problematic, particularly if the various Regulators had divergent views as to how the Proposed Rules should be applied and interpreted.
    - If a controlled group's holding company is a covered financial institution, its regulator should be the primary regulator.[2]
    - If a controlled group's holding company is not a covered financial institution, the Regulators should provide an objective basis for determining the identity of the group's primary regulator (*e.g.*, relative size of the covered financial institutions within the controlled group).
    - In addition, the annual report should only be required to be filed with the primary Regulator.
- If a controlled group's holding company is a covered financial institution, the provisions of the Proposed Rule that apply to executive officers should apply only to the executive officers of the holding company and not to the executive officers of each member of the controlled group that is a covered financial institution. A controlled group's policy decisions are almost always made at the holding company level, even though individuals other than the holding company executives may have some executive authority at the subsidiary level.
- The provisions of the Proposed Rules that apply specifically to "those covered persons (other than executive officers) who individually have the ability to expose the institution to possible losses that are substantial in relation to the institution's size, capital or overall risk tolerance" (referred to herein as "material risk-takers") should be based on the potential risk to the group as a whole and not the potential risk to each institution in the group that is a covered financial institution.

[2] The Regulators should also provide for flexibility in certain non-standard cases where the controlled group's holding company is a covered financial institution whose regulator might not be the appropriate primary regulator for the group. In those cases, the group's primary regulator might be determined based on the organizational structure of the group and the relative sizes of the covered financial institutions within the group.

Additionally, the Proposed Rules would apply to any subsidiary of any covered financial institution regulated by the Federal Reserve, regardless of the amount of such subsidiary's total consolidated assets. This provision is inconsistent with the statutory language in Section 956, as well as the Proposed Rules' implementation by the other regulators. For example, a subsidiary of a bank holding company that is engaged in a business line that is unrelated to financial services should not be subject to the Proposed Rules. The Regulators should clarify that the Proposed Rules do not apply to any subsidiary, regardless of Regulator, unless that subsidiary has total consolidated assets of at least $1 billion (or $50 billion, for the requirements applicable to larger covered financial institutions).

2. <u>Regulatory Review of Annual Reports</u>

The Regulators requested comment on the reporting provisions in the Proposed Rules, including whether the burden imposed on covered financial institutions was reasonable. It is imperative that covered financial institutions (and their employees) have finality in their compensation decisions. Therefore, the Regulators should clarify that, except in unusual circumstances, they will not require any retroactive changes to compensation design as a result of their review of the information disclosed in the annual reports.

3. <u>Scope of "Covered Person" Definition</u>

- *Materiality Threshold*

The Regulators requested comment on whether the Proposed Rules fulfill the requirement to obtain meaningful and useful descriptions of incentive-based compensation arrangements for supervisory and compliance purposes. Furthermore, the Regulators stated that the disclosure requirements in the Proposed Rules:

> are designed to help ensure that covered financial institutions will provide the [Regulators] with a streamlined set of materials that will help the [Regulators] promptly and effectively identify and address any areas of concern, rather than with voluminous materials that may obfuscate the actual structure and likely effects of an institution's incentive based compensation arrangements.

The Proposed Rules would require covered financial institutions to describe to the Regulators <u>any</u> incentive-based compensation arrangement paid to <u>any</u> employee. This would mean, for example, that a covered financial institution would be required to prepare a summary of incentive arrangements paid to the institution's IT personnel in connection with the completion of a new technology project and to bank tellers who are awarded "employee of the month" prizes at local branches. These types of arrangements are clearly not within the intended scope of Section 956 of the Dodd-Frank Act. A failure to limit the breadth of the disclosure being requested under the Proposed Rules will result in the Regulators receiving extensive amounts of information that is immaterial to the goals of the Proposed Rules and Section 956 and certainly will not result in a "streamlined set of materials" for Regulators to review. We suggest that the definition of "covered persons" for purposes of the disclosure requirement be limited to executive officers and those individuals whose actions, individually or in the aggregate, could have a material adverse impact on the covered financial institution's risk profile.

- *Definition of "Executive Officer"*

The Regulators also requested comment on the proposed definition of "executive officer." We believe that the Regulators should modify this definition in the following two ways:

- The Regulators should clarify, as discussed above, that only executive officers of a covered financial institution holding company are covered and not executive officers of each member of the controlled group that is a covered financial institution.

- The Regulators should revise the definition of "executive officer" in both the Proposed Rules and the June 2010 Interagency Guidance on Sound Incentive Compensation Policies (the "Interagency Guidance")[3] to conform to the existing definition in Rule 3b-7 of the Securities Exchange Act of 1934 (the "Exchange Act"). We do not see any meaningful benefit to the Regulators' proposed utilization of multiple definitions of the same term for the same purpose. Using the Exchange Act's definition of "executive officer" would have the benefit of allowing covered financial institutions to employ a definition with which they are already familiar, likely resulting in a more efficient regulatory process. The Exchange Act definition has long been used in the executive compensation context as part of the required disclosure under Item 402 of Regulation S-K, and it is therefore appropriate to use the definition in the context of review of incentive compensation arrangements as well.

- If the Regulators choose not to employ the Exchange Act definition of "executive officer," the Proposed Rules should at the very least conform its definition with the Interagency Guidance. The Interagency Guidance defines executive officers as "senior executives and others who are responsible for oversight of the organization's firm-wide activities or material business lines." The Proposed Rules, on the other hand, contemplate a new definition of "executive officer" based predominantly on title and/or job function, rather than responsibility. As discussed above, we do not see any policy reason for the same regulators to regulate the same entities for the same purpose with two different definitions of the same term. Although we think that using the Exchange Act definition would be the most consistent and efficient approach, the principles-based approach taken in the Interagency Guidance would at least allow each covered financial institution to apply the rules in a manner that is tailored to its particular structure and situation.

[3] 75 Fed. Reg. 36,395 (June 25, 2010), *available at* http://edocket.access.gpo.gov/2010/pdf/2010-15435.pdf.

- *Definition of "Covered Persons Presenting Particular Loss Exposure"*

The Proposed Rules require that the incentive compensation arrangements of certain "material risk-takers" be subject to review and approval by the board of directors of a covered financial institution with $50 billion or more in total consolidated assets. The Regulators requested comment on the scope of employees subject to this requirement. In response to this request, we suggest that the Regulators define this category of "material risk-takers" consistently with the definitions in the Interagency Guidance. The Proposed Rules refer to "those covered persons (other than executive officers) who individually have the ability to expose the institution to possible losses that are substantial in relation to the institution's size, capital or overall risk tolerance." The Interagency Guidance defines the same target group as "individual employees, including non-executive employees, whose activities may expose the organization to material amounts of risk (e.g., traders with large position limits relative to the organization's overall risk tolerance)". There does not appear to be any intended substantive difference between the two definitions, and since we think that the same purpose was intended by both definitions, we suggest that the Regulators continue to use the Interagency Guidance definition.

The Regulators should also clarify that, in the context of identifying material risk-takers, the board of directors or compensation committee of a covered financial institution is not required to identify these individuals itself, but instead must only establish appropriate procedures for the identification of material risk-takers and ensure that such procedures are implemented by the institution's management. Neither the board nor the compensation committee will necessarily be in a position to directly identify these individuals as efficiently or thoroughly as the institution's management; therefore, the Regulators should clarify that the board and the compensation committee can meet their duty with respect to the identification of material-risk takers under the Proposed Rules by relying on a report prepared by the institution's management in accordance with the procedures described above.

4. Scope of "Incentive-Based Compensation" Definition

- *Types of Incentive Compensation Covered*

In response to the Regulators' request for comment regarding the scope of their proposed definition of "incentive-based compensation," while we generally support the goal of implementing a principles-based definition allowing for sufficient flexibility, we believe that further clarification is required regarding the intended scope of this definition as it relates to the Proposed Rules' requirement that at least 50% of "the annual incentive-based compensation" of an executive officer be deferred over a period of no less than three years. The Regulators should clarify that this deferral requirement applies only to annual bonuses, and not (unless the covered financial institution elects otherwise) to: multiyear incentive performance arrangements; grants of options; or awards of restricted stock or restricted stock units ("RSUs") not tied to annual bonuses. In addition, the Proposed Rules should give covered financial institutions the flexibility to treat any particular award to a covered executive as "annual incentive-based compensation" subject to the deferral requirement even if the award would not automatically be deemed as such.

If the deferral requirement does apply to one or more of these types of awards, there are numerous interpretational issues that will need to be addressed:

- Confirm that the deferral period begins in the year of grant.
- With respect to options, if the deferral period begins in the year of grant, confirm that the deferral requirement would be satisfied by a three-year ratable vesting period.
- With respect to restricted stock and RSUs, confirm that the deferral requirement would be satisfied by a three-year ratable vesting period.
- For equity awards with performance-based vesting, confirm that the deferral requirement would be satisfied by a performance period of at least three years.

Additionally, while we assume that fixed sign-on and retention bonuses are not intended to fall within the scope of incentive-based compensation for purposes of the Proposed Rules (because such bonuses are not "variable compensation that serves as an incentive for performance"), specific examples explicitly confirming these conclusions should be included in the final regulations.

- *Treatment of Dividends and Appreciation*

Additionally, we believe that the Regulators need to review the following provision of the Proposed Rules that states that the proposed definition of "incentive-based compensation":

> would not include dividends paid and appreciation realized on stock or other equity instruments that are owned outright by a covered person. However, stock or other equity instruments awarded to a covered employee under a contract, arrangement, plan or benefit would not be considered owned outright while subject to any vesting or deferral arrangement (irrespective of whether such deferral is mandatory).

This statement creates the negative implication that dividends paid and appreciation realized on unvested and/or deferred equity awards <u>are</u> considered incentive-based compensation within the meaning of the Proposed Rules. We believe that the Regulators should specifically clarify that these items are <u>not</u> within the scope of the definition of incentive compensation. If dividends and appreciation are nevertheless included in the definition of deferred compensation, their inclusion should be limited to dividends and appreciation that represent above-market earnings. This would be consistent with the approach long taken by the SEC in its executive compensation reporting requirements. Absent above-market earnings, these amounts are no different than the amounts that could be earned if the investments were purchased by a third party on the open market.

If the Regulators do intend to include all or a portion of dividends paid or appreciation realized within the definition of "incentive-based compensation," a number of practical and logistical questions would need to be given further consideration.[4] These questions would best be addressed by ensuring that the deferral period commences on the date of the grant of the award giving rise to the dividends or appreciation, and that such dividends and appreciation are not themselves treated separately as additional incentive compensation subject to yet another three-year 50% deferral requirement.

5. **Prohibition on Excessive Compensation**

The Regulators requested comment on the factors that Section 956 directed be considered when determining whether compensation is excessive, including appropriate factors to consider in evaluating comparable compensation practices at comparable institutions for that purpose. The Proposed Rules should incorporate or acknowledge that the factors are not intended to set a level or range of compensation for directors, officers or employees.[5] The Proposed Rules should also acknowledge that the application of these factors by any particular covered financial institution to any particular employee involves the judgment of the institution's compensation committee and that, absent unusual circumstances, such judgment will not be subject to further review and comment by the Regulators if the compensation committee follows a deliberative process in good faith. Such an acknowledgement would be consistent with the additional emphasis placed on the independence of compensation committees by Section 952 of the Dodd-Frank Act.

6. **Implementation of Deferral Requirement**

- *Implementation of Deferral and Adjustment of Deferred Amounts*

The Regulators requested comment on all aspects of the scope and specific requirements of the deferral requirement in the Proposed Rules. While we believe that deferrals can play an extremely important role in providing proper risk based incentives (indeed, many of our members already have implemented deferrals for senior executives that would exceed those prescribed by the Proposed Rules), we do not believe that the Proposed Rules should contain a mandatory deferral requirement. The time and form of compensation should not be dictated by prescriptive rules imposed in a "one size fits all" manner. A mandatory, prescriptive deferral requirement:

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[4] For example:

- Would dividends paid and appreciation realized be subject to the same three-year 50% deferral requirement as other incentive-based compensation paid to executive officers?
- When would appreciation be realized for this purpose? On a mark to market basis or when paid out or vested? When would dividends be "paid" on a restricted stock unit that accrues dividend equivalents—when actually paid out, when vested or at some other time?
- Would these amounts be included in the "denominator" for purposes of determining the amount of compensation that constitutes the 50% of compensation that must be deferred?
- Are dividend equivalents treated in the same manner?

[5] *See* 12 USCA §1831p-1(d)(1), which further defines how the FDIC factors referenced in Section 956 are to be applied by the FDIC.

- is inconsistent with the flexible, principles-based approach of the Interagency Guidance, which states that "methods for achieving balanced compensation arrangements at one organization may not be effective in restraining incentives to engage in imprudent risk-taking at another organization. Each organization is responsible for ensuring that its incentive compensation arrangements are consistent with the safety and soundness of the organization." The mandate will not allow compensation committees of financial institutions to fully tailor their compensation structures to account for differences in the activities and risks associated with each executive officer's position within the institution and do not account for differences among institutions.

- is inconsistent with the statement in the Proposed Rules that "[m]ethods and practices for making compensation sensitive to risk-taking are likely to evolve during the next few years." The Proposed Rules would truncate the evolution which would otherwise inevitably occur by making deferrals the mandatory method of addressing risk adjustments to compensation. Mandating deferrals could also cause some institutions to increase base salary, making less of the total compensation subject to performance adjustments. It was only recently, after the Enron crisis, that there was substantial tax legislation (Section 409A of the Internal Revenue Code (the "Code")) designed to discourage, regulate and potentially penalize deferrals. Compensation committees need the flexibility to respond to changing circumstances, including new practices and changes in law.

- mandates a singular approach to risk management for the senior executives in spite of the fact that the Proposed Rules state that the "methods for achieving balance are not exclusive" and the Interagency Guidance stated that deferral was merely one of four non-exclusive methods that could be used to align incentive compensation with an organization's safety and soundness.

Each institution's compensation committee should continue to have the authority to determine precisely how the institution's compensation arrangements will comply with all applicable regulatory principles in a manner that is best suited for the needs of the institution. This includes the ability to determine which measures are appropriate to use as risk-based adjustment mechanisms for amounts of compensation that are deferred. While it may be useful to achieve these purposes by tying some individuals' deferred compensation to stock price, others' compensation may be more appropriately tied to performance of a business line. The compensation committee will also be in a better position to ensure that the arrangements are appropriate in light of other legal and regulatory constraints.

If the deferral requirement is to be retained, the Regulators should clarify that the deferral is only required to be implemented with respect to the aggregate "annual incentive-based compensation" paid to an executive officer, and that the deferral requirement need not be applied separately to each individual "annual incentive-based" award made to that executive.

- *Length of Deferral Period*

The Regulators requested comment on whether the minimum required deferral period should be extended beyond the currently proposed three years. As discussed above, we do not believe that the Proposed Rules should require any mandatory deferral period; however, if a deferral requirement is implemented, we do not think that it is necessary to impose a deferral period of longer than three years on incentive compensation paid to executive officers. A three-year deferral period is consistent with the suggested principles and standards set forth in other publications by global regulatory bodies on this topic, including the Financial Stability Board's Implementation Standards for its Principles for Sound Compensation Practices (the "Implementation Standards").[6]

An additional key issue that the Regulators should address is how the deferral requirement is affected by certain changes in employment status. We assume that the Regulators do not intend for the deferral requirement to continue to apply in the event of a situation such as death, disability, commencement of government employment, a change in control or certain cases of involuntary termination (*e.g.*, in connection with a divestiture or reduction in force). The Regulators should clarify that an individual can receive immediate accelerated payout of deferred amounts in the event that, for example, he or she leaves employment with the covered financial institution and becomes employed by the Federal Reserve and must comply with applicable conflict of interest rules.[7]

- *Potential Expansion of Scope of Covered Persons Subject to Deferral Requirement*

As currently drafted, the Proposed Rules' deferral requirement applicable to certain covered financial institutions with assets greater than $50 billion would apply to the institution's executive officers (as defined in the Proposed Rules). The Proposed Rules request comment on whether this deferral requirement should instead apply to a differently defined group of individuals, such as the institution's top 25 earners of incentive-based compensation. Because we do not believe that there should be any mandated form of compensation (as explained above), we do not believe that the mandate, if retained, should be expanded. Additionally, applying this rule to a group such as the top 25 earners would raise extremely difficult practical considerations, as many of our members (and the Federal Reserve) experienced in connection with interpreting and applying the TARP rules on executive compensation (the "TARP Rules").[8] For example, the group of top 25 earners would change each year, meaning that Regulators would need to clarify how the Proposed Rules would apply to individuals who were members of the top 25 one

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[6] *See* paragraph 7 of the Implementation Standards, available at www.financialstabilityboard.org/publications/r_090925c.pdf ("The deferral period described above should not be less than three years, provided that the period is correctly aligned with the nature of the business, its risks and the activities of the employee in question. Compensation payable under deferral arrangements should generally vest no faster than on a pro rata basis.")

[7] *See, e.g.*, Treas. Reg. § 1.409A-3(j)(4)(iii), which permits acceleration of deferred compensation in similar circumstances.

[8] *See* Interim Final Rule on TARP Standards for Compensation and Corporate Governance, *available at* http://www.treasury.gov/initiatives/financial-stability/about/Recipient_Guidance/executive-compensation/Documents/Interim%20Final%20Rule%20on%20Compensation%20and%20Corporate%20Governance.pdf.

year but not the next. Furthermore, institutions may not know who would become a top 25 earner at the time a relevant compensation arrangement is entered into.

- *Tax and Accounting Considerations*

The Regulators requested comment on any tax or accounting considerations that may affect the ability of covered financial institutions to comply with the proposed deferral/ex post adjustment requirement in the Proposed Rules. The Proposed Rules should provide that covered financial institutions may take into account applicable tax and accounting considerations in their compliance with the Proposed Rules. For example:

- Financial institutions should not be required to take any action that would result in the imposition of a penalty tax, or any other type of violation, under Sections 409A or 457A of the Code or any other similar tax law affecting deferred compensation.

- The ex post adjustment requirements in the Proposed Rules should not affect the ability of covered incentive compensation awards to qualify as "qualified performance-based compensation" pursuant to the rules under section 162(m) of the Code.

- From an accounting perspective, covered financial institutions should not be required to implement any deferral or ex-post adjustment mechanism that would result in liability accounting for equity awards. Under applicable accounting principles, an award is not "granted" unless the employee can understand all material terms of the grant. If an institution has too much discretion to reduce or forfeit an award (*e.g.*, if it grants an award of RSUs that is subject to reduction by the compensation committee with no objective criteria), the award will not be considered to have been granted and will be subject to liability accounting. Equity awards subject to liability accounting are recognized as liabilities, which are marked to market through earnings, and therefore create the additional adverse consequence of reducing capital and increasing liabilities.

7. <u>Clarify That Existing Awards Are Grandfathered</u>

The Regulators requested comment on the proposed compliance deadlines set forth in the Proposed Rules. The final regulations should clarify that any arrangements entered into prior to the effective date of the regulations will be grandfathered. In addition, the final regulations should provide for a specified transition period following their adoption to allow for orderly implementation.

8. <u>Board Review of Certain Incentive Compensation Arrangements</u>

The Regulators requested comments on the scope of the board of directors' review of incentive compensation arrangements for material risk-takers which requires that the board of directors should ensure that incentive compensation payment methods properly "make payments sensitive to <u>all</u> the risks arising from the covered person's activities, including those that may be difficult to predict, measure or model." (Emphasis added.) We believe that the board's review should be limited to risks that could reasonably be expected to have a potential material adverse impact on the covered financial institution (including any such material risk that is difficult to predict, measure or model). Requiring the board of directors to attempt to conceive and adjust compensation for every potential risk that may arise from an employee's activities is logically impossible and diminishes the board's ultimate ability to promote and foster the institution's overall business, safety and soundness.

9. <u>Personal Hedging Strategies</u>

The Regulators requested comment on whether the Proposed Rules should require covered financial institutions to specifically limit personal hedging strategies. We note that many of our members have long imposed such restrictions on the use of personal hedging strategies by employees in connection with incentive compensation programs and believe that such limits, in the discretion of the compensation committee, play an appropriate role in aligning compensation with risk outcomes. However, we do not believe that the Regulators should specifically prohibit the use of such strategies. This issue was specifically addressed by Section 955 of the Dodd-Frank Act, which directs the SEC to issue rules requiring issuers to disclose whether any employee or director is permitted to purchase financial instruments designed to hedge or offset any decrease in the market value of equity securities held by them or received as compensation. We do not think that it is necessary for the Regulators to further address this issue by imposing prohibitions when Congress only mandated disclosure. However, if the issue is addressed, we urge the Regulators to carefully limit any new rules to cover only those hedging strategies that are directly related to equity securities held for the purpose of achieving risk-related balance in compensation arrangements.

10. <u>Confidentiality of Information</u>

We commend the Regulators for recognizing the sensitivity of the information that covered financial institutions will be required to disclose on an annual basis to their regulators and pledging to maintain its confidentiality. We have frequently been concerned in recent years about the amount and scope of data that global regulators have suggested be publicly disclosed in the area of compensation, and we fail to understand how such disclosure to the public (fully available to every competitor) encourages prudent risk management or supports the safety and soundness of the institution. We fully support the Regulators' statement that they "generally will maintain the confidentiality of the information submitted to [them], and the information will be nonpublic to the extent permitted by law."

The Proposed Rules would require a covered financial institution to document its processes for establishing, implementing, modifying and monitoring incentive-based compensation arrangements. These documents would be expected to include, *e.g.*, copies of incentive-based compensation arrangements or plans, the names and titles of individuals covered by such arrangements or plans, records of the awards made under the arrangements or plans, and records reflecting the persons or units involved in the approval and ongoing monitoring of the arrangements or plans. To minimize the number of copies of confidential documents, we would suggest that the final regulation provide that the institution retain such documentation for inspection by the Regulator as necessary (rather than requiring such documentation to be submitted to the appropriate Regulator).

11. Determination of Asset Size for Investment Advisers

The Regulators requested comment on the proposed method of determining asset size for investment advisers. The Proposed Rules state that, for investment advisers, "asset size would be determined by the adviser's total assets shown on the balance sheet for the adviser's most recent fiscal year end." Under applicable accounting principles, an investment adviser acting as a general partner to a private equity or real estate fund must, in certain circumstances, consolidate the fund's assets on its balance sheet, even though those assets do not necessarily represent the actual equity interest of the investment adviser in the fund. The Regulators should clarify that, for purposes of determining an investment adviser's asset size under the Proposed Rules, the assets of a private fund managed by the adviser are required to be taken into account only to the extent of the adviser's equity in the fund.

12. Regulations vs. Guidelines

We request that the Regulators reconsider the format in which they have released the Proposed Rules. Section 956 of the Dodd-Frank Act called on the appropriate Federal regulators (as defined in Section 956) to jointly prescribe "regulations <u>or</u> guidelines" (emphasis added) with respect to additional compensation disclosure requirements and prohibitions on certain compensation arrangements. While we understand the need to structure the Proposed Rules' reporting requirements under Section 956(a) of the Dodd-Frank Act as rules since they require that the covered financial institutions actually file specific information with the Regulators, we believe that the substantive provisions contained in Section 956(b) of the Dodd-Frank Act, which are inherently more vague and require the application of discretion and judgment, should be implemented in the form of guidelines. This is particularly true with respect to controlled groups, which may be subject to oversight from more than one Regulator, as discussed above. Given the ongoing supervisory role of the Regulators contemplated by the Proposed Rules and the Interagency Guidance (which is in the form of guidelines and not rules), there should not be any concern that implementing the provisions of Section 956(b) as guidelines would diminish their efficacy. Additionally, even if the Proposed Rules are adopted partially in the form of guidelines, the Regulators will still have enforcement authority available to them under Section 505 of the Gramm-Leach-Bliley Act pursuant to Section 956(d) of the Dodd-Frank Act.

13. Relationship Between the Proposed Rules and the Interagency Guidance

The Proposed Rules and the Interagency Guidance are two attempts to deal with the same fundamental policy issues. We believe that the Interagency Guidance, in adhering to a principles-based approach coupled with effective supervision, have worked successfully to address the issues of concern to all parties involved. The Proposed Rules, issued by many of the same Regulators to address virtually the same issues as the Interagency Guidance, should be based on that Guidance. Requiring a covered financial institution to comply with two virtually duplicative, but somewhat inconsistent, sets of regulations to achieve the same policy goal is not the "least burdensome" method for achieving the relevant regulatory end.

We thank you for the opportunity to submit this comment letter. We would be happy to discuss with you any of the comments described above or any other matters you feel would be helpful in your evaluation of the Proposed Rules and the comments you receive. Please do not hesitate to contact the undersigned at (202) 962-7400 or via email at kbentsen@sifma.org or Lisa Bleier at (202) 962-7329 or lbleier@sifma.org if you would like to discuss these matters further.

Sincerely,

Kenneth E. Bentsen, Jr.
Executive Vice President,
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