FDIC reveals plans to crack down on executive pay

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The US Federal Deposit Insurance Corporation (FDIC) is seeking to increase levies on banks with short-term compensation policies, under proposed rules released for comment yesterday.

The FDIC cites a recent study by Harvard researchers Lucian Bebchuk, Alma Cohen and Holger Spamann into pay at the failed banks Lehman Brothers and Bear Stearns, which found that senior executives at both banks received a total of $2.4 billion via unrecoverable bonus payments and stock sales in the eight years leading up to the banks' collapse in 2008. According to the FDIC, this suggests "the executives' pay arrangements provided them with excessive risk-taking incentives", and contrasts with the fate of shareholders in both banks, who lost most of their investment.

The proposed rules would focus on equity compensation for employees who are responsible for taking significant risks and also receive substantial performance bonuses. Firms would be encouraged (by the prospect of lower FDIC levies) to pay "a significant portion" of total compensation to these employees in the form of restricted stock, which would become accessible only over a period of several years, and which could be clawed back if necessary.

Other regulators in the US and elsewhere have already proposed new limits on compensation, but the FDIC's plans are deliberately intended to raise the bar. While other regulations would create a compulsory minimum standard, the FDIC says its proposals will incentivise banks to adopt standards that exceed these supervisory minimums, in the same way its risk-based fees already do in other areas. Companies that meet the FDIC standards would pay lower levies than others, the regulator proposes – either through a reduction in the levy or the imposition of additional levies on non-compliant companies.

Neither the Fed nor the FDIC has suggested figures for the proposed limits on compensation. Though the international Financial Stability Board suggested last year up to 60% of compensation should be deferred, with 50% paid in stock or options, the Fed has questioned whether this would actually help stability.

After publication, the proposals will be open for comment for 30 days.