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Client Alert

Banking Regulators Offer Final Guidance on Sound Incentive Compensation Policies

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On June 21, 2010, the Federal Reserve, FDIC, OCC, and OTS jointly issued final guidance regarding incentive compensation and risk management at banking organizations. These agencies had previously issued proposed guidance on the subject in October 2009. The final guidance emphasized three core principles for incentive compensation programs in banking organizations:

- Incentive compensation programs should provide employees incentives that appropriately balance risk and financial results in a manner that does not encourage employees to expose their organizations to imprudent risk;
- The programs should be compatible with effective controls and risk-management; and
- The programs should be supported by strong corporate governance, including active and effective oversight by the organization's board of directors.

The final guidance does not implement any specific formulas or requirements, instead focusing on principles that banking organizations should rely upon in setting their policies. The final guidance covers not only "senior executives" but also any employee who may expose the organization to material risk. The agencies emphasized several points about incentive compensation, including:

- "One size fits all" approaches to incentive compensation are not ideal and each employee's compensation package should be viewed in light of the risk that employee might create;
- Incentive compensation should focus on the long-term performance of the organization and the employee; and
- Awards should often be deferred for extended periods of time so that performance can be more effectively evaluated.

If you have any questions regarding the final guidance, including how it applies to you or would like a copy of the final guidance, please contact your regular Vorys attorney or a member of the Vorys Financial Institutions group at any of the offices listed.