

Dodd-Frank Update: Incentive Compensation for Financial Institutions

May 13, 2016 | Client Update | 2-minute read

On Monday, May 2, 2016, the Federal Reserve and, on Friday, May 6, 2016, the SEC issued their versions of a repropose rule to regulate incentive compensation at the financial institutions under their purview, as required by Section 956 of the Dodd-Frank Act. These issuances follow the releases in the prior weeks of the proposed rule by the National Credit Union Administration, the Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency and the Federal Housing Finance Agency. We reported on the release of the proposed rule in our [visual memorandum](#) released last Monday.

As a [reminder](#), Section 956 of Dodd-Frank generally requires that these agencies jointly issue rules that:

- (1) prohibit incentive compensation that encourages inappropriate risks by certain financial institutions by providing excessive compensation or that could lead to material financial loss; and
- (2) require those financial institutions to disclose information concerning incentive compensation to the appropriate federal regulator.

The rules proposed by the six agencies are virtually identical, and differences are largely attributable to the specific regulatory mandates of each agency.

The [SEC version of the rule](#) is of particular note, because, as required, it contains a 130+ page economic analysis of the potential costs and benefits of the proposed rule. In doing so, the SEC considered the compliance costs of the proposed rule, which they were unable to fully quantify, and queried the possibility that the proposed rule could adversely impact otherwise beneficial risk-taking, “result in losses of managerial talent” and lead to the increase in total remuneration to compensate for the burdens imposed by the proposed rule.

The SEC acknowledged that it lacks full data as to current incentive compensation arrangements for all covered institutions and covered persons. Thus, as a proxy, the SEC relied on the supervisory experience of the other regulators and third-party academic research and tried to extrapolate from the compensation information publicly available for named executive officers. Not surprisingly, the SEC did not reach firm conclusions regarding the economic impact of the proposed rule and has invited comments supported by data and analysis addressing the issues discussed in its economic analysis.

On Wednesday, May 25, 2016, Davis Polk will host a webcast that will discuss the impact of the proposed rule.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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