Dodd-Frank Section 956 – The Financial Services Incentive Compensation Rules

Significant Changes Are Needed to 2016 Re-Proposed Rule to Prevent Devastating the Recruitment and Retention Prospects of Financial Services Firm

What are the Financial Services Incentive Compensation Rules? Dodd-Frank Section 956, the Financial Services Incentive Compensation rules were promulgated as a direct response to the belief that financial services incentive compensation plans contributed to inappropriate risk-taking that led to the 2008 financial collapse and is the first statutory mandate to impose significant constraints on Board decision-making on executive compensation. Section 956 charged a coalition of six federal regulators, including the Treasury, OCC, FDIC, and SEC to conduct a joint-rulemaking subjecting all regulated financial services firms to the requirements.

In 2011, the six regulator coalition proposed rules implementing Section 956. After over five years, a re-proposal was issued in April of 2016. As proposed, financial institutions with total consolidated assets over $1 billion dollars will be subject to restrictions designed to prevent companies from awarding incentive compensation deemed "excessive" or which encourages risk taking potentially leading to a material financial harm as well as onerous record-keeping requirements. For financial services firms with total consolidated assets exceeding $50 billion, the re-proposal provides for significant restrictions on the incentive compensation awarded to executive officers and "significant-risk takers" – a new term of employee which is intended to cover employees with the ability to subject the firm to risk. The restriction on these individuals include mandatory deferral periods of up to 60% of incentive compensation for a period of four years in addition to mandatory forfeitures and placing incentive compensation at risk for up to 11 years.

What is the Status? A re-proposal of a rule implementing Section 956 was offered in April of 2016 and there were rumors that the Obama Administration was trying to get the six regulator coalition to complete a final rule prior to his leaving office. However, the SEC as well as the NCUA currently lack the requisite agency leaders to properly vote and approve new rules and thus a final rule was not completed.

The Center's Position – The Center believes that the proper balancing and oversight of risk in incentive compensation plan design is a fundamentally important compensation and governance objective necessary to maximize shareholder benefit and drive company performance. However, the current proposal of the implementation of Section 956 eschews a focus on risk and instead focuses on the form of compensation as well as compensation magnitude. The result is an excessively over-inclusive regulation which covers employees and incentive plans that have no potential of creating material risk and, as a result, imposes extreme recruitment and retention hardships on financial services firms who will be competing for employees with companies in other industries where individuals will not be subject to the compensation restrictions imposed by Section 956.

The Recommended Course of Action – The Center supports a repeal of Section 956 or a re-proposal of the rule which aligns the implementation of Section 956 with the 2010 FDIC Safety and Soundness Standards in Incentive Compensation.