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The Special Master for TARP Executive Compensation Issues First Rulings

Today, the Special Master for TARP Executive Compensation Kenneth R. Feinberg released determinations on the compensation packages for the top executives at firms that received exceptional TARP assistance. Under the Emergency Economic Stabilization Act (EESA) as amended in 2009, the Special Master has a mandate to review all forms of compensation for five most senior executive officers and the next 20 most highly compensated employees at the seven firms that received exceptional TARP assistance (AIG, Citigroup, Bank of America, Chrysler, GM, GMAC and Chrysler Financial).

The determinations announced today for the top 25 most highly paid at the seven firms receiving exceptional assistance:

1. *Reform Pay Practices for Top Executives to Align Compensation With Long-Term Value Creation and Financial Stability*

· Reject cash bonuses based on short-term performance, as required by statute, in favor of company stock that must be held for the long term

· Restructure existing cash "guarantees" into stock that must be held for the long term

2. *Significantly Reduces Compensation Across the Board*

· Average cash compensation down by more than 90 percent

· Approved cash salary limited to $500,000 for more than 90 percent of relevant employees

· Average total compensation down by more than 50 percent

· Exceptions where necessary to retain talent and protect taxpayer interests

3. *Require Salaries to Be Paid in Company Stock Held Stock Over the Long Term*

· Stock is immediately vested, requiring executives to invest their own funds alongside taxpayers

· Stock may only be sold in one-third installments beginning in 2011--or, if earlier, when TARP is repaid--aligning executives' interests with those of taxpayers

4. *Require Incentive Compensation to be Paid in the Form of Long Term Restricted Stock – and to be Contingent on Performance and on TARP Repayment*

· Require executives to meet goals set in consultation with the Special Master, and certification of achievement of goals by an independent compensation committee

· Any incentives granted paid only in stock that requires three years of service and can be cashed in only when TARP is repaid

5. *Require Immediate Reform of Practices Not Aligned with Shareholder and Taxpayer Interests*

· Limits "other" compensation and perquisites

· No further accruals under supplemental executive retirement plans or severance plans

1. ***Reforms Pay Practices for Top Executives to Align Compensation Practices With Long-Term Value Creation and Financial Stability:*** The Special

Master's rulings represent a fundamental transformation from the pay practices of the past. These decisions will significantly alter the way that executives covered by the Special Master's decisions--including the senior executive officers and next 20 most highly compensated employees of each of the seven recipients of "exceptional" assistance under the TARP (AIG, Citigroup, Bank of America, Chrysler, GM, GMAC and Chrysler Financial)--are paid.

· ***Rejects Cash Payments Based on Short-Term Performance, as required by statute*****:** Traditionally, compensation for these employees has included large cash amounts, including significant cash bonuses. These payments gave executives incentives to take short-term risks and little reason to protect the long-term the health of the company or financial stability. After today's rulings, as required by statute and Treasury regulations, these executives will receive the overwhelming majority of their pay in company stock that may only be sold over the long term, aligning their interests with those of taxpayers and shareholders.

· ***Restructures Existing "Guaranteed" Cash Payments into Stock Held For the Long Term:*** Under the pay practices of the past, several executives in this group were awarded cash "guarantees" in 2009. Guaranteed minimum amounts give employees little downside risk in the event of poor performance--but upside when times are good. The Special Master required these agreements to be restructured. Under today's rulings, these amounts will be paid in company stock that must be held over the long term.

· ***Citigroup and Phibro:*** At Phibro, Citigroup's commodities trading unit, the Chief Executive Officer was to receive a significant cash bonus based on the short-term results of significant risk-taking. The Special Master rejected this approach, and Citigroup agreed to sell Phibro to a company that has not received taxpayer funds. Under today's ruling, nothing may be paid to the Phibro CEO until the sale is complete.

2. ***<u>Significantly Reduces Compensation Across the Board:</u>*** To break from the pay practices of the past, the Special Master has reduced compensation across the board--both in terms of cash and the total compensation executives will receive.

· ***On Average, Cash Compensation Decreased by More Than 90 percent*****:** The Special Master rejected cash payments based on short-term results that may prove illusory, and cash guarantees that separate pay from performance. Overall, the Special Master reduced cash pay by more than 90 percent from 2008 levels--and, as required by Treasury regulations, cash bonuses may no longer be paid to any of these employees.

· ***Approved cash salary generally limited to $500,000*****:** Consistent with the Administration's February 4 guidance on executive compensation at TARP recipients, the Special Master approved base salaries of $500,000 or less for more than 90 percent of the employees in this group. Base salaries greater than $1 million were approved in just three cases: for the new CEO of AIG, as previously announced, and for two employees of Chrysler Financial, which will wind down its operations in the near term and cannot grant employees long-term incentives.

· ***On Average, Total Compensation Decreased by More Than 50 percent*****:** Even including the value of stock that must be held for the long term, the Special Master reduced the total compensation packages for executives in this group to less than half of 2008 levels.

· ***Exceptions Where Necessary to Retain Talent and Protect Taxpayer Interests*****:** Although the Special Master's rulings generally emphasize decreases in both cash and total compensation across the seven companies, increases in compensation were permitted where shown to be necessary to retaining key talent critical to a company's long-term success--and, ultimately, ability to repay the taxpayer.

3. ***<u>Requires Salaries to be Paid in Company Stock Held Over the Long Term:</u>*** The Special Master's rulings fundamentally change the structure of compensation at these firms. Rather than cash, today's rulings require that the majority of salaries be paid in stock that must be held for the long term--giving executives incentives to pursue long-term value creation and financial stability.

· ***Stock is Immediately Vested, Requiring Executives to Put Their Own Funds at Stake:*** Rather than just cash, executives will earn base salaries in the form of vested stock in their companies. In effect, the Special Master is requiring each executive to invest their base salary in the long-term future of the firm, alongside taxpayers. These structures ensure that executives do not have incentives to take the excessive risks that contributed to the financial crisis.

· ***Stock May Only Be Sold in One-Third Installments, Beginning in Two Years:*** Unlike the pay practices of the past, which allowed executives to sell stock in their companies immediately, the Special Master's rulings require stock to be held for the long term. Stock received as salary may only be sold in one-third installments that will not begin until 2011, unless the taxpayer is repaid earlier.

4. Require Incentive Compensation to be Paid in the Form of Long Term Restricted Stock – and to be Contingent on Performance and on TARP Repayment: As the Secretary noted in his June 10 statement, incentive pay can be undermined by compensation practices that set the performance bar too low or simply reward rising tides. The Special Master's rulings require that incentives be paid only if executives reach objective goals agreed upon in consultation with the Special Master--and only if TARP is repaid.

· ***Requires Achievement of Goals Set in Consultation with the Special Master:*** The Special Master's rulings permit these executives to receive incentive pay only if the executives attain objective, predetermined performance goals set in consultation with the Special Master. Achievement of these goals must be certified by each company's compensation committee--which, under Treasury regulations, must be composed solely of directors fully independent from management.

· ***Requires Three Years of Service, and TARP Repaid, Before Payment:*** To ensure that taxpayers continue to receive the benefits of the executives' talents, the Special Master's ruling requires that any incentive awards be paid only if the employee provides at least three years of service to the company after the award is made. And, under Treasury regulations, the awards must be paid in the form of restricted stock that may not be paid unless the company repays its TARP obligations.

5. ***Requires Immediate Reform of Practices Not Aligned With Shareholder Interests:*** As the Secretary noted in his June 10 statement, in some cases golden parachutes and supplemental executive retirement plans have expanded beyond their original purpose, and may not enhance the long-term value of the firm or allow shareholders to easily ascertain the full value of the "walkaway" pay an executive will receive when departing the firm. The Special Master's rulings place tough new restrictions on these payments--as well as perquisites and other personal benefits--for executives at companies that have received exceptional taxpayer assistance.

· ***Caps perquisites and "other" compensation:*** Several experts, including the Conference Board Task Force on Executive Compensation, have concluded that executives--and not companies--should generally cover the costs of personal expenses. The Special Master's rulings generally cap these types of payments at $25,000, with limited exceptions for unusual circumstances that can be justified to the Special Master.

· ***Additional limitations on "golden parachute" payments:*** Large "golden parachute" or severance payments often serve to enrich executives rather than provide reasonable compensation during unemployment, and often do not enhance the long-term value of a company. Tough new Treasury regulations prohibit these payments to the senior executive officers and five most highly compensated employees at all companies that have received taxpayer assistance. The Special Master's rulings go further, however, and prohibit companies from increasing the amount of any "golden parachute" payable to any of the top 20 most highly compensated executives during 2009.

· ***Freezing supplemental executive retirement plans:*** Supplemental executive retirement benefits can provide substantial cash guarantees to departing executives, regardless of performance. And, as the Secretary noted on June 10, these complex benefits can make it difficult for shareholders--and, in the case of exceptional assistance companies, taxpayers--to ascertain the full amount of pay an executive will receive upon retirement. The Special Master's rulings conclude that that executives should provide for their retirements with wealth based on performance while they are employed, rather than being guaranteed substantial retirement benefits beyond those provided to everyday workers. As a result, the Special Master's decisions prohibit additional accruals under supplemental executive pension programs and company credits to other non-qualified deferred compensation plans following the release of today's rulings.

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LINKS

- Executive Compensation Determinations for Top TARP Recipients