

**Towers Watson
Monthly Regulatory Round-Up**

January 2010

-- Executive Compensation --

The Monthly Regulatory Round-Up is a high-level summary of legal and regulatory developments that occurred during January 2010 that may be relevant to large employers. Developments are sorted according to

- federal legislative developments,
- federal regulatory guidance
- other developments (e.g., significant litigation, studies, select state law developments).

The Monthly Regulatory Round-Up is prepared by Towers Watson's Technical Services staff, located in Valhalla, NY. This material is not a substitute for legal, accounting, actuarial or other professional advice.

REGULATORY

1. ***Higher FDIC premiums contemplated for banks with risky pay programs.*** The Board of Directors of the Federal Deposit Insurance Corporation (FDIC) approved an Advance Notice of Proposed Rulemaking (ANPR) requesting comments on whether insured depository institutions with risky employee compensation structures should pay higher premiums to the deposit insurance program. The ANPR includes a broad set of questions about whether and how employee compensation should be factored into the risk-based pricing system and the types of compensation structures that should be encouraged. The ANPR indicates that a compensation model that would meet FDIC standards may include the following features:

- A significant portion of the compensation for employees whose business activities can present significant risk to the institution would be paid in restricted, non-discounted company stock.
- Significant awards of company stock would only become vested over a multi-year period, subject to a look-back mechanism (e.g., clawback) to account for the outcome of risks assumed in earlier periods.
- The employee compensation program would be administered by a committee of the Board composed of independent directors with input from independent compensation professionals.

2. ***IRS correction program for 409A NQDC plan document failures.*** The IRS issued Notice 2010-6, which permits taxpayers to correct certain failures of a nonqualified deferred compensation plan to comply with the plan document requirements of IRC § 409A. The types of relief provided for document failures include the following:

- Transition relief allows document failures identified in the Notice to be corrected by December 31, 2010 (if certain conditions are met), generally without any income inclusion or application of the 20% tax under IRC § 409A for those covered under the arrangement.
- Plan terms identified in the Notice may be corrected at any time without income inclusion or the 20% tax, if the provision being modified does not affect actual operation of the plan for a period of one year following the correction. If this condition is not fulfilled, relief is still available to limit the amount that must be included in income and the additional taxes.
- The Notice clarifies that certain ambiguous, but relatively common phrases found in plan documents will not be treated as causing the plan to violate IRC § 409A. Examples are phrases like "as soon as practicable" and "termination of employment," but only if there is no pattern or practice of interpreting the phrase in a manner that is inconsistent with the requirements of IRC § 409A.
- Correction of document failures can be made without any income inclusion or application of the 20% tax during a limited period after the adoption of a new plan, provided the plan is the first one of that type ever maintained by the employer (applying the nine plan "types" set forth in the 409A regulations for this purpose), disregarding grandfathered arrangements and plans under which all amounts have been paid or forfeited.

The relief in Notice 2010-6 is not available to stock options or stock appreciation rights and is available to certain linked plans only on a transition basis through 2011. The Notice also clarifies certain aspects of Notice 2008-113, which addresses failures of nonqualified deferred compensation plans to comply with IRC § 409A in operation.

3. **Say-on-pay rules for TARP companies.** The SEC adopted amendments to the proxy rules implementing the requirement under the Emergency Economic Stabilization Act of 2008 (EESA) for U.S. registrants that have received financial assistance under the Troubled Asset Relief Program (TARP) to give shareholders a non-binding vote on executive compensation (i.e., say-on-pay) during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding.

OTHER

1. **CCGG model say-on-pay policy.** The Canadian Coalition for Good Governance (CCGG) released its Model Shareholder Engagement and “Say on Pay” Policy for Boards of Directors. The model policy is intended “to provide guidance to boards on their engagement with shareholders, expected disclosure on their approach to executive compensation, a recommended form of shareholder advisory resolution and what can be done by the board with the results of the vote.” The model policy is available at: <http://www.ccgq.ca/site/ccgg/assets/pdf/CCGG-Say-on-Pay-Final.pdf>.
2. **FSB begins “peer review” process regarding implementation of their sound compensation principles and standards.** The Financial Stability Board (FSB) is currently conducting a peer review of implementation of the Principles and Standards for Sound Compensation Practices, which were endorsed by the G20 Leaders at their Summits in London in April 2009 and Pittsburgh in September 2009. The review will focus on the steps being taken or planned by FSB members to ensure effective application of the Principles and Standards, as well as progress to date in implementation by significant financial institutions. The review is to be completed by March 2010, as requested by G20 Leaders. A template to collect information from national authorities was distributed to FSB members and the responses will be analyzed and discussed by the FSB. The template is available at: http://www.financialstabilityboard.org/press/pr_100109b.pdf.