Entities which have received money through the Troubled Asset Relief Program ("TARP") must take note of recently released guidance from the Department of Treasury ("Department"), because it clarifies changes in the way certain employees can be compensated. On June 15, 2009, the Department's interim final rule regarding standards for executive compensation and corporate governance under TARP was published in the Federal Register. The rule is available at http://edocket.access.gpo.gov/2009/pdf/E9-13868.pdf.

THE BASICS
Section 111(b) of the Emergency Economic Stabilization Act of 2008 ("EESA") places limitations on compensation of certain individuals by entities that receive money through TARP. 12 U.S.C.S. § 5221(b) (2009). Specifically, "during the period in which any obligation arising from financial assistance provided under TARP remains outstanding," a TARP recipient cannot:

• compensate senior executive officers with incentives that encourage them to "take unnecessary and excessive risks that threaten the value" of the company (12 U.S.C.S. § 5221(b)(3)(A));

• make any "golden parachute" payments to a senior executive officer or any of the next five most highly compensated employees (12 U.S.C.S. § 5221(b)(3)(C)); or

• pay or accrue any bonus, retention award, or incentive compensation, unless the payment is made pursuant to a valid employment agreement executed before February 11, 2009 (12 U.S.C.S. § 5221(b)(3)(D)).

Further, Section 111(b)(3)(B) gives a TARP recipient, or the government, the power to recover from senior executive officers any bonus, retention award, or incentive compensation which was based on materially inaccurate statements of earnings, revenues, gains, or other criteria (12 U.S.C.S. § 5221(b)(3)(B)).

Section 111(f) requires the Secretary of the Treasury ("Secretary") to review compensation paid to senior executive officers and the next 20 most highly compensated employees before February 17, 2009 "to determine whether any such payments were inconsistent with the purposes of this section or the TARP or were otherwise contrary to the public interest." This section also gives the Secretary the authority to seek from the TARP recipient and the employee reimbursement of compensation determined to be inappropriate. The Secretary must make this determination in accordance with the principles outlined in Section 111(b).

Additional points of note are Section 111's requirements that TARP recipients create a "Board Compensation Committee" to review compensation plans (12 U.S.C.S. § 5221(c)); limitations on luxury expenditures (12 U.S.C.S. § 5221(d)); and requirement of shareholder approval of executive compensation (12 U.S.C.S. § 5221(e)).

CAVEATS
The prohibition on payment of bonuses, retention awards, or incentive compensation under Section 111(b) does not apply to payment of certain long-term restricted stock or in instances where the bonus is "required to be paid pursuant to a written employment contract executed on or before February 11, 2009, as such valid employment contracts are determined by the Secretary [of the Treasury] or the designee of the Secretary." 12 U.S.C.S. § 5221(b)(3)(D)(i),(iii). The rule also makes clear that

1. The term "senior executive officer" encompasses an entity's Chief Executive Officer; the four most highly compensated officers aside from the CEO; and up to two additional individuals for whom disclosure of compensation would have been required under federal securities laws, but for the fact that they were not serving as executive officers at the end of the previous fiscal year.
the exclusion for contracts executed before February 11, 2009 applies only to such contracts as they read on that date. Any changes made to the contract after February 11, 2009 will be subject to Section 111(b)(3)(D). For example, if a contract executed before February 11, 2009 is amended after that date to add a bonus not previously included, that bonus would likely be barred by Section 111(3)(D)’s prohibition on bonus payments.

Moreover, the individuals to whom the bonus payment prohibition applies vary depending on the amount of money the entity receives from TARP. 12 U.S.C.S. § 5221(b)(3)(D)(ii). If the entity receives less than $25,000,000, the prohibition applies only to the single most highly paid employee; if the entity receives between $25,000,000 and $250,000,000, the prohibition applies to at least the five most highly paid employees (the Secretary has the discretion to apply it to others); if the entity receives between $250,000,000 and $500,000,000, the prohibition applies to all senior executive officers and at least the 10 next most highly paid employees; and if the entity receives $500,000,000 or more, the prohibition applies to senior executive officers and at least the 20 next most highly paid employees.

An additional caveat contained in the interim final rule is that the Special Master (appointed by the Secretary to help ensure EESA compliance) may examine payments made pursuant to contracts executed before February 11, 2009 and “provide an advisory opinion . . . stating whether such payments are consistent with the [American Recovery and Reinvestment Act] or EESA, or are otherwise contrary to public policy . . . and may seek reimbursement of such payments where appropriate.”

**ADDITIONAL STANDARDS**

Section 111(h) gives the Secretary the authority to establish additional standards of compensation and corporate governance. The interim final rule explains that the Secretary has established four such standards:

- Entities that receive “exceptional financial assistance” must submit “the compensation payments and compensation structures of the senior executive officers and most highly compensated employees subject to the bonus payment limitation, and the compensation structures of all other executive officers and 100 most highly employees,” for approval by the Special Master.
- All TARP recipients must “disclose to the Treasury and its primary federal regulator annually any perquisites whose total value exceeds $25,000 for any employee who is subject to the limitations on bonus payments.”
- All TARP recipients must disclose to the Treasury and its primary federal regulator whether it has engaged a compensation consultant within the past three years, and if so, the types of services the consultant provided.
- No TARP recipient can provide to any of its senior executive officers and the next 20 most highly compensated employees reimbursements of taxes owed in relation to severance payments, perquisites, or any other form of compensation.

**ACTION ITEM**

Entities which have received TARP funds should consult with their employment attorney to ensure that their compensation plans comply with the EESA.

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2. The interim final rule defines “exceptional financial assistance” as “any financial assistance provided under the Programs for Systemically Significant Failing Institutions, the Targeted Investment Program, the Automotive Industry Financing Program, and any new program designated by the Secretary as providing exceptional financial assistance.”