



LEGAL ALERT

October 26, 2009

Federal Reserve Board Issues Guidance on Incentive Compensation Arrangements for Banking Organizations

On October 22, 2009, the Federal Reserve Board (the "FRB") issued 45 pages of proposed guidance to all banking organizations on incentive compensation practices (the "Guidance") which it found to be one of several factors contributing to the current financial crisis.

The Guidance addresses (1) incentive compensation arrangements, (2) the role of risk management, and (3) the role of the board of directors. Pursuant to the Guidance, incentive compensation arrangements must be structured properly for all employees at a banking organization, including non-executive employees, who have the ability, either individually or as a group, to take material risks. The compensation arrangements must be balanced and tailored.

The Guidance also states that a banking organization should have strong controls governing its process for designing, implementing and monitoring incentive compensation arrangements. Further, a banking organization should conduct regular internal reviews to ensure that its processes for achieving and maintaining balanced incentive compensation arrangements are followed consistently. Among other things, the Guidance affirms the Board's responsibility to review and approve the overall goals and purposes of the organization's incentive compensation system.

While acknowledging that the issues surrounding incentive compensation are complex, the FRB stated its commitment "to moving banking organizations forward to incorporate the principles described in this guidance into incentive compensation practices" and urged banking

organizations to commit adequate resources to the task.

The FRB also has directed its supervisory staff to review incentive compensation arrangements at community and regional banking organizations as part of the regular, risk-focused supervisory process. Supervisory findings will be included in the relevant report of examination or inspections, communicated to the organization, and incorporated, as appropriate, into the organization's supervisory rating. The FRB, in appropriate circumstances, may take enforcement action against a banking organization if its incentive compensation arrangements or related risk management, control or governance processes pose a risk to the safety and soundness of the organization and the organization is not taking prompt and effective measures to correct the deficiencies.

For more specific information regarding complying with the Guidance, you may contact the following individuals of our office at (717) 731-1700 or the email addresses below.

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To learn more about the Guidance and best practices, register to attend Bybel Rutledge LLP's 2010 SEC and Corporate Governance Conference which will be held on November 18, 2009 at the Hershey Country Club, Hershey, Pa. For more information visit our website or contact Nancy J. Runk of our office at runk@bybelrutledge.com.

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