

## CLIENT UPDATE

### Treasury Appoints Special Master to Approve Compensation Arrangements For Recipients of “Exceptional” TARP Assistance

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Acting under a rule it had adopted in June to implement executive compensation restrictions for financial institutions receiving assistance under the federal government’s Troubled Asset Relief Program, the Treasury Department named Kenneth R. Feinberg as the Special Master to review compensation and governance standards of those institutions.

The Special Master is given the following powers and authority:

- Compensation Design.
  - Senior Executive Officers and Most Highly Compensated Employees. For those TARP recipients receiving “exceptional assistance”, the Special Master will set compensation for its five senior executives and the next 20 most highly-compensated employees. If the compensation structure is materially modified by the TARP recipient after it has been approved by the Special Master, it must be reapproved.
  - Other Executive Officers and Most Highly Compensated Employees. The Special Master will also review compensation arrangements for those employees of TARP recipients receiving “exceptional assistance” who are either executive officers or one of the 100 most highly compensated employees (excluding those covered by the first bullet above). The Special Master must determine whether compensation is adequately structured, but is not required to set amounts. Again, if materially modified after approval, it must be reapproved.
  - Safe Harbor. Compensation arrangements will automatically be deemed to comply with TARP requirements without prior approval by the Special Master if the annual compensation payable to an employee is not more than \$500,000, and any additional compensation is paid in the form of long-term restricted stock.
  - Principles to be Applied by Special Master. In reviewing compensation design to determine whether it is consistent with applicable pay controls, the Special Master is to consider:
    - Risk: Compensation should avoid incentives that reward employees for taking unnecessary or excessive risks that could threaten the value of the TARP recipient;

- Taxpayer Return: Compensation should reflect the TARP recipient's need to remain competitive, retain and recruit talented employees, and be able to repay TARP monies;
  - Appropriate Allocation: Compensation should be properly allocated among salary, short- and long-term incentives, and cash, equity or other types of compensation;
  - Performance-based Compensation: An appropriate portion of compensation should be performance-based through tailored metrics over a relevant performance period;
  - Comparable Structures and Payments: Compensation should be proportionate to amounts paid to individuals in similar positions at similarly situated companies; and
  - Employee Contribution to TARP Recipient Value: Compensation should reflect the current or future contributions of an employee to the TARP recipient's value.
- Review of Prior Payments to Employees. The Special Master is responsible for reviewing bonuses, retention awards and other compensation paid before February 17, 2009, to determine whether such payments were inconsistent with the applicable pay controls or otherwise contrary to public policy and, if so, for negotiating with the TARP recipient (even TARP recipients that did not receive exceptional assistance) and the offending employee for appropriate reimbursements to the Federal Government.
  - Advisory Opinions. The Special Master is authorized to render advisory opinions as to whether a compensation structure is, will or may result in payments that are inconsistent with the applicable pay controls or otherwise contrary to the public interest.

The rule creating the office of Special Master, issued under the recent American Recovery and Reinvestment Act of 2009, which in turn amended 2008's Emergency Economic Stabilization Act, adopts additional standards (filling in several previously existing loopholes) and consolidates executive compensation related provisions directed at TARP recipients in a single rule. Prior to becoming the Special Master, Mr. Feinberg was a well-known mediator.

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