

Aldrich Bonnefin & Moore, PLC

[CORPORATE GOVERNANCE UPDATE]

MAY 2011

PROPOSED RULE ON INCENTIVE COMPENSATION ISSUED

Pursuant to the Dodd-Frank Reform Act, the federal financial regulatory agencies issued a proposed rule to ensure that regulated financial institutions' incentive compensation agreements do not encourage inappropriate risks. The proposed rule is centered around three key principles: (1) incentive compensation arrangements should appropriately balance risk and financial rewards; (2) be compatible with effective controls and risk management; and (3) be supported by strong corporate governance. The proposed rule is intended to complement the agencies' previously issued guidance on sound incentive compensation policies that was issued in June 2010.

The proposed rule would apply to financial institutions with assets of \$1 billion or more (covered institutions). These covered institutions would be required to establish policies and procedures that ensure compliance with the proposed rule. Further, covered institutions would be required to provide certain information about their incentive compensation arrangements, which would have to be submitted to the institution's federal regulator. The largest of financial institutions (generally those with \$50 billion or more in assets) would be subject to heightened standards, including a requirement to defer the payment of at least 50 percent of an executive officer's incentive compensation for at least three years and that the amounts ultimately paid in the end reflect losses or other features of performance

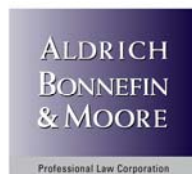
over time. In general, an "executive officer" would be defined under the proposal as a person who holds the title or performs the function (regardless of title, salary or compensation) of one or more of the following positions: president, chief executive officer, executive chairman, chief operating officer, chief financial officer, chief investment officer, chief legal officer, chief lending officer, chief risk officer or head of a major business line.

If a final rule is adopted, the agencies propose to make the terms of the rule effective six months after publication in the Federal Register, with annual reports due within 90 days of the end of each covered financial institution's fiscal year.

A copy of the proposed rule can be obtained from each of the banking, thrift and credit union agency's website, including the FRB's website at www.federalreserve.gov/newsevents/press/bcreg/20110330a.htm.

AGENCIES ISSUE PROPOSED CREDIT RISK- RETENTION RULES

In March, 2011, the Federal banking agencies, the Securities and Exchange Commission, the Federal Housing Finance Agency and the Department of Housing and Urban Development (the Agencies) issued a Notice of Proposed Rulemaking (Proposed Rules) to implement the credit risk retention requirements of Section 941 of the Dodd-Frank Reform Act. Section 941 generally



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requires the securitizer of asset-backed securities to retain not less than five percent of the credit risk of the assets collateralizing the asset-backed securities.

Section 941 includes a variety of exemptions from these requirements, including an exemption for asset-backed securities that are collateralized exclusively by “qualified residential mortgages” (e.g., traditional fixed rate purchase loans with 80 percent LTV and good borrower credit) and certain other asset classes, such as auto loans and commercial loans.

The comment period for the Proposed Rules ends June 10, 2011. The full text of the Proposed Rules can be found at: www.fdic.gov/news/board/29Marchno2.pdf.

SMALL BUSINESS LENDING FUND APPLICATION DEADLINE EXTENDED UNTIL MAY 16, 2011

The U.S. Treasury announced on March 30 that it has extended the C- Corporation application deadline for the Small Business Lending Fund from March 31, 2011 to May 16, 2011 (at midnight, Eastern Time). Treasury did not offer any reason for the move, and noted that for S- Corporations, the term sheet and application deadline will be announced at some later date.

Treasury has also indicated that it expects to begin approving applicants in the “coming weeks.”

INTERSTATE BRANCHING EASED FOR STATE MEMBER BANKS.

On February 14, the Federal Reserve Board issued Supervisory Letter SR 11-3 regarding the Dodd-Frank Reform Act provisions that modified federal law governing de novo interstate branching. A result of the Reform Act a state member bank is now authorized to open its initial branch in a host state by establishing a de novo branch at any location at which a bank chartered by the host state could establish a branch. The Supervisory Letter can be found at <http://www.federalreserve.gov/boarddocs/srletters/2011/sr1103.htm>.

TARP AUDITORS WITH GUNS?

Most bankers would be surprised to hear that the Office of the Special Inspector General for the Troubled Asset Relief Program (SIGTARP), which is responsible for overseeing and auditing the Troubled Asset Relief Program, has been designated to be a law enforcement agency. The SIGTARP office employs investigators who are empowered with carrying guns and badges, have recently requested police car upgrades, and have already performed raids in coordination with other law enforcement agencies. So next time that a SIGTARP agent walks into your bank, be nice.