

Employee Benefits Alert: Executive Compensation Significantly Restricted by Economic Stimulus Package

2/19/2009

On February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Tax Act of 2009 (the "Act"), which amended the Troubled Asset Relief Program (TARP). The Act restricts executive compensation payable by TARP recipients in numerous ways, including, but not limited to:

- imposing limits on compensation payments to the five highest paid officers to ensure there are no incentives to take unnecessary and excessive risks that may threaten the value of the TARP recipient;

- providing for a "clawback" of any bonus, retention award, or incentive compensation payment to the 25 highest-paid employees if the payments were based on statements of earnings, revenues or other criteria that are later found to be materially inaccurate;

- prohibiting *any* severance payments to the ten highest paid employees, which is defined broadly to include *any payment* made to a departing employee, except payments for services performed or benefits accrued;

- generally prohibiting the payment of *any* bonuses, retention awards or incentive compensation, except that long-term restricted stock grants are permissible, provided a grant does not exceed one-third the value of the grantee's annual compensation and does not fully vest while any obligation arising out of the TARP assistance remains outstanding; note, however:

 - the application of this restriction to particular classes of employees in financial institutions depends on the level of assistance received: the single most highly compensated employee in institutions that received less than \$25,000,000; the five most highly compensated employees for institutions that received at least \$25,000,000 but less than \$250,000,000; the 15 most highly compensated employees in institutions that received at least \$250,000,000 but less than \$500,000,000; and the top 25 employees for those that received \$500,000,000 or more; and

 - this prohibition does not apply to any bonus required to be paid by an employment agreement executed on or before February 11, 2009;

- prohibiting any compensation plan that encourages earnings manipulation;

- requiring CEOs and CFOs to certify compliance with the Act;

- requiring that a company-wide policy concerning excessive or luxury expenditures be adopted;

- requiring that any proxy or consent or authorization for an annual or other meeting of shareholders include a nonbinding "say-on-pay" shareholder resolution to approve executives' compensation; and

- requiring that the board of directors establish a compensation committee that:

 - consists exclusively of outside directors (except in the case of a nonpublic company receiving less than \$25,000,000 in assistance, in which case the board must perform compensation committee functions);

 - is responsible for reviewing recipients' compensation plans; and

 - meets semiannually to review such plans.

In addition, the Act directs the Treasury Secretary to review bonuses, retention awards and other compensation paid to recipients' top 25 employees *before* February 17, 2009 to determine whether any such payments were inconsistent with the Act's purposes. If the Secretary concludes they were, the TARP recipient and service provider shall be obligated to negotiate for reimbursement of the funds.

Generally, the Act's proscriptions apply to the period of time in which a recipient of TARP funds owes any obligation arising out of any financial assistance received, except the period during which the federal government holds only warrants to purchase the recipient's common stock.

For assistance in this area, please contact one of the attorneys listed below or any member of your Mintz Levin client service team.

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