John Pesh
Director, Executive Benefits
Telephone: 608.665.8223
E-mail: john.pesh@cunamutual.com
Fax: 608.236.7356

CUNA MUTUAL GROUP
INSURANCE • SERVICES • ASSET MANAGEMENT

July 21, 2016

Gerard S. Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Delivered Electronically

RE: Proposed Rule, Incentive-Based Compensation Arrangements 12 CFR Parts 741 and 751; RIN 3133-AE48

Dear Mr. Poliquin:

On behalf of CUNA Mutual Group, I am pleased to provide comments on the re-proposed rule on incentive-based compensation arrangements. CUNA Mutual is the nation's leading provider of financial products and services to credit unions and credit union members. Specifically, in relation to this rule, CUNA Mutual makes available various executive benefit programs as well as several member financial services and products which, in some instances, may be supported by incentive-based compensation arrangements.

The overall purpose of the proposed rule is important. Excessive compensation and incentive-based compensation which puts credit unions at undue risk of material loss should be closely scrutinized and generally not permitted. In our view, the proposed rule is too onerous in its current form. As proposed, the rule places credit unions, along with the broader financial services and banking industries, at risk of losing talented individuals who are both qualified and capable of appropriate risk-taking while also managing the safety of their respective business. Further, as drafted, the rule challenges credit unions and talented leaders in their ability to innovate and keep pace with the ever-evolving needs of the members these institutions and individuals are charged to serve.

The Proposed Rule Challenges Appropriate Risk Taking
The terms of the proposed rule require the majority of compensation to covered persons be deferred for up to three years, pending the results of business decisions. Once paid, that compensation is then subject to clawback provisions for up to an additional seven years. In total, under the proposed rule, compensation to a credit union's Senior Executive Officers and Significant Risk Takers is at risk for up to a full 10 years, an unreasonably long time in our view. During this time, a myriad of potential variables can impact the results of earlier decisions. Moreover, while many decisions may be appropriate and well thought-out at the time, other conditions, changes, or actors may ultimately be more responsible for adverse consequences, a result for which the proposed rule does not seem to account. Decisions may be undermined by inappropriate decisions by successive employees, with potential for no impact on the

compensation of such successive actors. In fact, later serving individuals could potentially benefit if their own compensation plans include incentives, for such things as expense reduction, which could motivate an individual to undermine the efforts of a predecessor. In short, this extreme duration of risk may result in decision-makers who make only those decisions perceived to be risk-free, or as close as possible to risk-free, in order to preserve their personal compensation for the long-term. Such decisions may be to the detriment of innovation and are likely to limit even the most appropriate risk-taking.

It is our recommendation that the duration for which compensation is at risk be shortened to a maximum of five years total, which covers the majority of a business cycle as described in the proposed rule. This duration should include a deferral period of up to three years, and a maximum clawback period of two years. This five year duration also coincides with common employment practices putting credit unions and other financial institutions on equal footing with other industries[1, 2]. To supplement and improve the oversight process, CUNA Mutual encourages focused attention on documentation and review of the decision-making process as opposed to the results. A shortened at-risk period, coupled with an emphasis on process, cuts to the heart of the proposed rule whereby the intent is to promote good decisions where incentive-based compensation is potentially a motivator.

In addition, CUNA Mutual is concerned the criteria used to determine a forfeiture or downward adjustment is still overly broad. The concept that downward adjustments or forfeitures can happen as a result of “other aspects of conduct or poor performance, as defined by the covered institution” casts an extremely wide net if the definitions are not explicit. Causing compensation to be at risk for factors unrelated to performance extends outside of the scope of the rule and may, in application, violate some state wage laws. We recommend that this language either be removed from the proposed rule or, if included, stipulate a defined trigger in the incentive-based compensation plans and specific to the performance of the plan.

The Proposed Rule Underestimates Time and Expense Required
While the U.S. Securities and Exchange Commission (SEC) proposal includes an estimate of the additional time and expense required by the rule, the other agencies failed to include this important analysis. Further, while an important attempt, the SEC’s figures do not appear to adequately consider the potential additional time and expense required for compliance with the proposed rule. In addition, the rule does not make reference to many of the existing, related rules and regulations that also require compliance. Likewise, the same requirement for deferrals of compensation is likely to trigger compliance with Internal Revenue Code Sections 457 and 409A given the complexity of deferred compensation arrangements now required for all covered persons. To ensure plans in compliance with the rule, employers will likely be required to hire additional consultants, attorneys, and Certified Public Accountants to obtain the necessary knowledge and maintain ongoing compliance.

Adding further cost and complication, the proposed regulation presupposes the clawback provision is easily enforceable. Enforcing a clawback for a period of seven years is likely to require significant costs to enforce collection, assuming the clawback provision is enforceable in the location where the employee or former employee is located and the former employee has the ability to repay.

CUNA Mutual recommends a more thorough analysis of the potential downstream compliance costs by each of the agencies. This analysis should consider the fact that, at least for federal credit unions, incentive-based plans are already regulated by existing rules. For example, NCUA Rule 701.21(c)(8)(iii)(C) and Rule 721.7(b)(3) regulate incentive payments to an employee, other than a senior management employee, in connection with a loan or any incidental powers activity. After such analysis, if the additional compliance costs are found to outweigh the benefits, a revised proposal should be drafted and opened for additional public comment.

In summary, CUNA Mutual recommends the NCUA consider the impact the proposed incentive compensation rule may have on innovation and appropriate risk-taking at credit unions. We also recommend the NCUA analyze the significant compliance costs for credit unions in order to estimate the additional time and expense required to implement the rule which has not yet been studied in detail.

Thank you for your consideration of these comments and recommendations. Should you have any questions regarding this submission, please do not hesitate to contact me.

Sincerely,

John Pesh
Director, Executive Benefits

[1] The report entitled Clawbacks: Trends and Developments in Executive Compensation by Katherine Blostein of Outten & Golden, LLP, as published by the American Bar Association on March 25, 2010 notes changes in clawback practices as a result of Sarbanes-Oxley Act of 2002, the American Recovery and Reinvestment Act of 2009, and overall trends in response to regulators and shareholders concerns. This report identifies specific concerns related to the use of clawbacks, including legality in many states and enforceability, and specifies that vesting and clawback durations have generally grown from three years to five years.

[2] On July 1, 2015, the SEC issued Proposed Rule 10D-1 relating to clawbacks pursuant to Section 10D of the Securities and Exchange Act of 1934 in response to Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. This proposed rule imposed a 3 year clawback requirement, which has been largely adopted by public companies. The 2016 Trends and Developments in Executive Compensation report by Meridian Compensation Partners indicates that 40% of companies are already in compliance with this rule.