SIFMA
Securities Industry and
Financial Markets Association

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SIFMA Guidelines for Compensation

The Securities Industry and Financial Markets Association ("SIFMA") has prepared these Guidelines for Compensation in coordination with other industry groups and compensation and governance professionals.

These Guidelines reflect a focused commitment of the industry to structure compensation arrangements to discourage inappropriate risk-taking. These Guidelines recognize that each firm must provide oversight through its Board of Directors or Compensation Committee. This oversight authority is ultimately responsible for the firm's compensation practices and for implementing any changes to firm policies in light of the specific business needs and risk tolerance of the firm and its lines of business as well as the long-term interests of shareholders.

The global nature of the financial services industry requires that regulatory initiatives be complementary and well coordinated. Any regulatory agency – such as a systemic risk regulator – should focus on facilitating practices that will help firms enhance risk-taking measurements and encourage the industry to operate dynamically and help drive economic growth. It is vital that financial services firms are not restricted from attracting, motivating and retaining the necessary talent to make them successful.

Finally, the Guidelines encourage transparency, while respecting confidentiality. Transparency assists shareholders and other investors in understanding a firm's compensation structure, risk control processes, and business strategy. At the same time, appropriate confidentiality is necessary to ensure competitive differentiation among firms is maintained and personal privacy is respected.

1. The Firm Should Establish Compensation Policies Consistent With Effective Risk Management.

Compensation policies can best promote growth and stability if they are aligned with the interests of shareholders and the long-term profitability of the firm. As part of this, limits on excessive risk-taking begin with a sound business strategy that does not encourage employees to take excessive risk and appropriate policies and controls at the business level to ensure excessive risk is not taken. Compensation policies and practices should support a firm's overall approach to risk management and are one aspect that Boards of Directors must take into account in creating an appropriate culture of compliance and risk management. The Board of Directors or the Compensation Committee should be able to:

- Consult periodically with risk and/or compliance staff ("risk management professionals") to provide input independent of the relevant business line on how compensation relates to risk at various levels in the organization.
- Have access to an independent compensation consultant hired by them.
- Have access to information from sources other than management about effective compensation and risk control practices.

Directors who are independent of management should be responsible for the determination that the firm's compensation programs do not incentivize excessive risk-taking.

2. Compensation Should be Linked to Sustainable Performance.

The Compensation Committee, or another sub-committee of the Board of Directors exercising oversight authority, should be responsible for reviewing compensation policies with the objective of providing appropriate incentives to achieve the performance goals set by it on a sustainable basis. Compensation determinations must be based on the facts and circumstances of the particular firm and the particular employees or executives involved; for example, compensation considerations relating to senior management or employees that can materially impact the business may call for one solution whereas compensation for other employees may call for another. The oversight authority may employ various mechanisms in setting compensation in order to link that compensation to sustainable performance and the long-term interests of shareholders.

- The amount of compensation should take into account individual, business unit and overall entity performance for the relevant compensation period.
- The Compensation Committee should have significant discretion to adjust a senior manager's compensation to reflect both financial factors (for example liquidity risk, cost of capital, reputation risk and the time horizon of risks) and non-financial factors (for example compliance, risk management and management development). The mix of quantitative and qualitative factors to be considered in determining compensation will depend on the particular circumstances, and the appropriate balance will likely vary among firms and lines of business.
- Where compensation is based on performance that may be difficult to estimate, may entail longer-term consequences to the employer that cannot be reliably measured in the shorter-term, or is based on expected future-year revenue, that compensation may be subjected to repayment, vesting or other similar mechanisms or time horizons that reflect those risks.
- Where appropriate, a meaningful portion of compensation should be awarded in the form of employer equity that is paid in the future or required to be held for a significant period of time to better align employee incentives with the long-term interests of shareholders.

3. Risk Management Professionals Should Be Appropriately Independent.

Risk management is the responsibility of business units and risk management professionals working closely to ensure that risk is appropriately identified, measured, priced and managed. Risk management is critically important for each firm and for the financial system as a whole. Accordingly, each firm should seek to establish a culture that continually invests in and is guided by strong risk management, judgment and controls. Toward this end, the compensation of risk management professionals must encourage the effective implementation of risk controls and risk monitoring.

- Risk management professionals should have appropriate access to the Board and the Compensation Committee.
- Risk management professionals should have a reporting line independent of the units they oversee to the senior risk officer of a major line of business or to the chief risk officer for the firm.
- Compensation for risk management professionals should be based on the achievement of objectives linked to their functions and determined independently of business areas.
- Risk management professionals should have stature commensurate with the importance of the risk oversight function, and compensation should establish and/or maintain that stature.

4. Firms Should Communicate Their Compensation Practices to Shareholders.

The compensation practices of the firm should include a description of the company's compensation philosophy and, in particular, how the compensation policies and practices are designed so as not to incentivize excessive risk-taking. That disclosure should address the manner in which the employer's compensation system contributes to sustainable performance of the company within the risk parameters established by the Board of Directors or the Compensation Committee. That disclosure should not extend to individual employee compensation disclosure (except as required under SEC rules for named executive officers) for reasons of privacy and competitiveness. For public firms, this disclosure could be a component of the currently required Compensation Discussion and Analysis, which requires an explanation of the compensation philosophy and decisions of a public company with respect to its senior executive officers.