# <u>The Special Master's Proposed "Brake" Provision</u>:

**What is being proposed?**
The proposal is for institutions to adopt a policy giving their board and compensation committee the authority, in a crisis situation, to restructure, reduce or cancel pending payments to executives. Under such a policy, contracts like employment agreements and stock option agreements would have special language providing for this authority.

**Who is it proposed for?**
The Special Master proposed it directly to seventeen firms, but it is proposed for consideration by other firms as well.

**How does a policy get adopted?**
A company would decide to adopt a policy on an entirely voluntary basis. The Special Master has proposed a set of adoption standards that provide discretion for a company to tailor a policy to its particular circumstances.

**What is a "crisis situation" and who decides?**
The proposal contemplates a crisis as extraordinary adverse circumstances that constitute a significant threat to the financial viability of a company. Whether such circumstances exist is for a company's board to decide.

**Who would such a policy cover?**
A group of senior leaders and highest-earning employees (which will include all executive officers) selected by the company.

**What kind of arrangements would a policy apply to?**
Generally, to cash and stock incentive plans and awards, executive retirement programs and "golden parachute" arrangements.

**Is the policy a "clawback"?**
No. The "brake" would allow a company to restructure, reduce or cancel payments that haven't been made when the brake is triggered, but is not intended for recovery of payments made before that time.

**What could a compensation committee do if the "brake" was triggered?**
The committee would have a range of options, such as reducing or canceling the amount of a payment, delivering a payment in stock instead of cash (and requiring that stock to be held), or adding additional performance criteria. In some circumstances, tax and accounting considerations would make giving the committee absolute authority impractical, so appropriate limitations on range of options would be necessary.

**What has to be disclosed?**
Companies adopting a policy would describe the adoption in a current securities filing. The proposal also provides for descriptions of a company's implementation process in its annual proxy filing—number of employees covered, etc.— and updated disclosure if the company amends or rescinds its policy.

**Office of the Special Master for TARP Executive Compensation**
**ADOPTION STANDARDS FOR PROPOSED COMPENSATION POLICY**

1. Purpose. The policy purpose is to establish and preserve the compensation committee's discretion to exercise superseding authority over compensation arrangements of covered employees during a covered period, notwithstanding limitations on its authority outside of a covered period. The policy will be administered and interpreted by the compensation committee, in its sole discretion.

2. Superseding authority. Provide for superseding authority to be comprehensive, including the authority to cancel or reduce the amount of any payment, require a payment be delivered in any combination of cash or property, add a condition to or defer the vesting or delivery of any payment, or restrict the transferability of any payment delivered in vested property.

3. Limitations of authority. To the extent that comprehensive superseding authority would violate a statute or government regulation, or result in substantial adverse tax or accounting consequences, the authority may be limited to the extent necessary to avoid such a result. For example, if providing comprehensive superseding authority would result in an arrangement failing to meet the requirements of Section 409A of the Internal Revenue Code, or would result in a share-based payment intended to be classified as equity instead being classified as a liability, limiting authority in such an arrangement is appropriate. The company shall seek in good faith to minimize limitations.

4. Covered period. A covered period is a period of time during which there are extraordinary adverse circumstances that constitute a significant threat to the financial viability of the company. The company's board of directors has the authority, in its sole discretion, to determine the existence or cessation of extraordinary adverse circumstances.

5. Covered employees. The population of employees covered by the policy will be a group of senior leaders and highest-earning employees identified by the company and will include executive officers.

6. Compensation arrangements. A compensation arrangement is any plan, program or agreement (or an award or grant under such a plan, program or agreement) providing for compensation of any type required to be disclosed under Item 402 of Regulation S-K, except for the following: salary, tax-qualified retirement benefits, "other" compensation arising from reasonable relocation or expatriate expenses, elective deferrals of compensation, programs provided to salaried employees generally in which the level of benefits is not determined by the employee's level of compensation, and programs that provide a *de minimis* amount of compensation.

7. Implementation of the policy. The policy applies to all compensation arrangements established after the adoption of the policy with any person who is then a covered employee. Any such policy shall provide expressly for superseding authority during a covered period, unless the committee has the equivalent of such authority under any conditions and circumstances. In addition, if rights or entitlements in existence prior to an individual becoming a covered employee either limit or preclude the company from unilaterally obtaining superseding authority in a compensation arrangement, upon such individual becoming a covered employee the company will consider whether it should seek to obtain such authority, including by conditioning eligibility for prospective compensation arrangements on the delivery of consent to obtain such authority.

8. Disclosure. In addition to any other disclosure requirements in respect of the policy, the company will file a current report on its adoption and describe the policy in the company's next Compensation Discussion & Analysis. The description will include: a statement of the policy; the status of its implementation; the number of covered employees and the rationale for selecting that population and groups in that population; circumstances in which superseding authority was limited and the rationale for the limitation. In any subsequent Compensation Discussion & Analysis, the company will update those descriptions (or, as the case may be, confirm the absence of updates) and describe other amendments to the policy and its implementation. In the event the company rescinds, or establishes a material limitation or exception to, the policy, it will be disclosed in a current report along with the rationale for doing so.