



EXECUTIVE COMPENSATION CLIENT ALERT

STIMULUS BILL AFFECTS EXECUTIVE COMPENSATION OF TARP PARTICIPANTS

February 16, 2009

President Obama is expected to sign the American Recovery and Reinvestment Act of 2009 (the “Recovery Act”) tomorrow. The Recovery Act has significant implications on the compensation arrangements of institutions that have accepted or will accept government funds under the Emergency Economic Stabilization Act’s Troubled Assets Relief Program (“TARP”). The Recovery Act affects all TARP recipients, including those that have previously received TARP funds.

TREASURY SECRETARY TO ESTABLISH COMPENSATION GUIDELINES

The Recovery Act directs the Treasury Secretary to establish standards and promulgate regulations on executive compensation practices of TARP recipients. It is not clear if the new standards are effective immediately or if they will be effective after further guidance from the Treasury Secretary. While the Treasury Secretary is given broad power in the Recovery Act to establish new executive compensation guidelines, the standards must include at least the following restrictions:

Bonus, Retention and Incentive Compensation Payments Drastically Restricted. A TARP recipient is prohibited from paying or accruing any bonus, retention award or incentive compensation to certain highly compensated employees. The restriction is phased in by the amount of TARP assistance received by the entity as follows:

Amount of Financial Assistance Received Under TARP	Persons Unable To Receive Bonus, Retention Awards or Incentive Compensation
Less than \$25,000,000	Most highly compensated employee
At least \$25,000,000 but less than \$250,000,000	Five most highly compensated employees
At least \$250,000,000 but less than \$500,000,000	Top five senior executive officers and the 10 next most highly compensated employees*
\$500,000,000 or more	Top five senior executive officers and the 20 next most highly compensated employees*

*The Treasury Secretary may increase this number if determined to be in the public interest.

Notwithstanding the restrictions in the table above, bonus payments are permitted if paid under a written contract executed on or before February 11, 2009. Also, bonus, retention or incentive compensation



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may be paid in the form of restricted stock but only if: (i) the stock does not fully vest during the period in which any TARP obligation remains outstanding; (ii) the stock does not exceed one-third of the executive's total annual compensation; and (iii) the grant is subject to any other terms and conditions that the Treasury Secretary determines are in the public interest.

Severance Payments Limited. TARP limited golden parachute payments to the top five senior executive officers, generally defining a golden parachute payment as a payment on account of an involuntary departure from a company. The Recovery Act expands the application of the golden parachute limitations to apply also to the next five most highly compensated employees of the TARP recipient, and the term "golden parachute payment" is defined to include any payment for departure from a company for any reason, except for payments for services performed or benefits accrued.

Expanded Compensation Clawbacks. TARP required financial institutions to recover any bonus, retention award, or incentive compensation paid to any one of the top five senior executive officers based on statements of earnings, revenues, gains, or other criteria that are found to be materially inaccurate. The Recovery Act expands this rule to apply to the next 20 most highly compensated employees of a TARP recipient.

Compensation May Not Encourage Manipulation of Earnings. The Recovery Act prohibits any compensation plan that would encourage manipulation of the reported earnings of a TARP recipient to enhance the compensation of any of its employees.

Compensation Committee Membership. Companies receiving TARP assistance must create a compensation committee of the board of directors that is established entirely of independent directors. The compensation committee must meet at least semiannually to discuss and evaluate employee compensation plans in light of the TARP requirements. If the TARP recipient is privately held and received \$25,000,000 or less in TARP assistance, the duties of the compensation committee under TARP must be carried out by the entire board of directors.

RECOVERY ACT IMPOSES ADDITIONAL COMPENSATION RESTRICTIONS

In addition to the standards described above that the Treasury Secretary must establish, the Recovery Act affects executive compensation in these ways:

CEO and CFO Certifications. The chief executive officer and chief financial officer of a TARP recipient must provide a written certification of compliance with the executive compensation restrictions described in TARP and modified by the Recovery Act. If the TARP recipient is a publicly traded corporation, the certification must be provided to the Securities and Exchange Commission. Privately held corporations must make the certification to the Treasury Secretary.

Limitations on Luxury Expenditures. The Recovery Act requires the board of directors of a TARP recipient to have a company-wide policy regarding excessive or luxury expenditures. This includes policies on entertainment, events, office and facility renovations, air and other travel and other activities or events that are not reasonable expenditures for staff development, reasonable performance incentives or other similar measures conducted in the normal course of business.

Say on Pay Vote by Shareholders. Shareholders of a TARP recipient may require a separate shareholder vote at each annual or other shareholder meeting to approve the compensation of executives,



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although the vote is not binding on the TARP recipient's board of directors. The Securities and Exchange Commission is directed to issue guidance on this requirement within one year.

Treasury Secretary To Review Prior Compensation Payments. The Treasury Secretary is directed to review compensation paid to the top five senior executive officers and the next 20 most highly compensated employees of an entity receiving TARP assistance before the date of enactment of the Recovery Act to determine whether the payments were inconsistent with the provisions of the new law affecting executive compensation, TARP or otherwise contrary to the public interest. The Treasury Secretary is empowered to negotiate reimbursements to the federal government with respect to any excess payments.

Expanded Compensation Deduction Limit. TARP limited the amount of deductible compensation paid to senior executive officers of certain financial institutions. The Recovery Act expands the scope of the \$500,000 compensation deduction limit. Under the Recovery Act, the \$500,000 limit applies to any entity that will receive TARP assistance regardless of the type or amount of assistance.

Withdrawal of TARP Participation. Any institution that has already received TARP funds may repay the assistance and the Treasury Secretary will liquidate its warrants at current market prices. A financial institution taking advantage of this right may repay the assistance with funds from any source and will no longer be subject to the executive compensation restrictions of TARP.

ACTION ITEMS

TARP recipients should evaluate the impact the new restrictions will have on their executive compensation practices as changes are likely needed. For more information regarding the executive compensation restrictions of the Recovery Act, contact your regular Kutak Rock representative or any member of our Executive Compensation and Employee Benefits practice group listed below. For more information on our Executive Compensation and Employee Benefits practice, please visit us at www.kutakrock.com.



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