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BANK REGULATION

Agencies Should Finalize Rulemaking on Incentive Compensation

GAO Highlights

Highlights of GAO-25-107032, a report to the Ranking Member, Committee on Financial Services, House of Representatives

Why GAO Did This Study

Incentive-based compensation can motivate good performance but also encourage risky behavior. Bank failures in early 2023 and executive bonuses one bank paid on the day it failed raised questions about compensation practices at large banks.

GAO was asked to review compensation at three failed banks. This report examines (1) executive compensation packages at the failed banks and a peer bank group, (2) executives' stock transactions at the failed banks, (3) regulators' review of executive compensation at selected large banks, and (4) efforts to finalize an incentive compensation rule.

GAO analyzed the most recent publicly available annual disclosures for 11 banks (three failed banks and eight peer banks selected for similarity in asset size and business lines); public disclosures on stock transactions by executives at the failed banks (January 2021–March 2023); and examination documentation (2017–2022) on compensation for 21 banks (10 banks with largest asset size, eight peer banks, and three failed banks). GAO also reviewed agencies' proposed rules and public statements on the incentive compensation rulemaking since 2011.

What GAO Recommends

GAO is making six recommendations—one to each agency required to issue incentive compensation regulations—to jointly prescribe regulations or guidelines as soon as practicable. Each agency agreed with the recommendation.

View GAO-25-107032. For more information, contact Michael E. Clements at (202) 512-8678 or clementsm@gao.gov.

What GAO Found

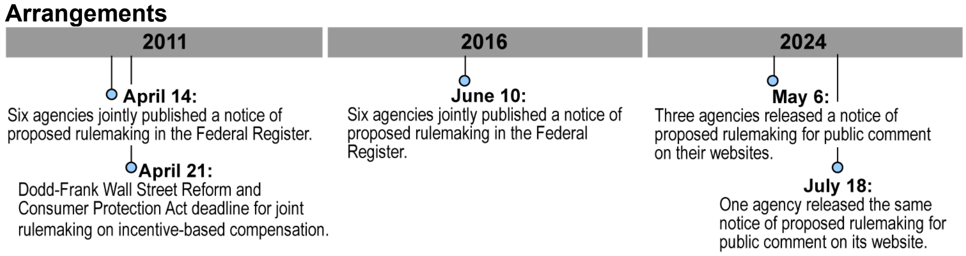
The structure and amount of executive compensation packages at three failed banks were similar to those of peer banks GAO reviewed. A median of 86 percent of executive compensation at the failed banks and 83 percent at the peer banks was incentive-based and tied to executive and bank performance. All the packages incorporated risk-mitigating elements that align with practices described in federal compensation guidelines. All the banks used financial measures of performance, such as return on equity and shareholder returns. Most banks also used nonfinancial measures, such as meeting goals for prudent risk management.

All the former top executive officers at the three failed banks received stock awards (totaling about $130 million) and made disposals (totaling about $214 million) from January 2021 through March 2023. Executives at two of the failed banks disposed of more than $17 million in the first quarter of 2023, which was similar to their disposals in the first quarter of the previous year.

Federal banking regulators use supervisory activities, such as ongoing monitoring and examinations, to review compensation issues and risks at large banks. From 2017 through 2022, regulators examined executive compensation at 15 of the 21 large banks GAO reviewed, including two of the three failed banks. Overall, regulators identified 10 supervisory concerns (matters requiring attention) related to compensation issues across eight institutions during this period. This included one supervisory concern in 2022 at the holding company of one of the failed banks, which was taking corrective action when the bank failed.

In 2010, Congress required six agencies to jointly prescribe regulations or guidelines on incentive compensation by April 21, 2011. The agencies formed a working group to draft and propose joint regulations but have yet to finalize them (see figure).

Timeline of Key Events Related to Rulemaking on Incentive-Based Compensation Arrangements



Source: GAO analysis of statute and proposed rules. | GAO-25-107032

Leaders within and across the agencies hold differing views on regulatory approaches for incentive-based compensation arrangements. For example, some agency leaders advocate a principles-based approach that outlines general principles and objectives for discouraging inappropriate risk-taking. Others support an approach with more specific and stringent requirements. Reconciling these differences and jointly prescribing regulations or guidelines would help prevent excessive compensation arrangements at financial institutions that encourage inappropriate risks.