Lessons Learned Oral History Project Interview

Interviewee Name and Crisis Position	Kenneth Feinberg[1] US Treasury Special master for TARP executive compensation
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Introduction

The Yale Program on Financial Stability (YPFS) interviewed Mr. Kenneth Feinberg regarding his time as the special master for Troubled Assets Relief Program (TARP) executive compensation. In this role, Mr. Feinberg was tasked with overseeing the revision of executive payments in companies that received exceptional TARP assistance during the Global Financial Crisis of 2007–2009. These revisions applied to the executives of American International Group, Citigroup, Bank of America, General Motors, General Motors Acceptance Corporation (GMAC), Chrysler, and Chrysler Financial.

For four decades, Mr. Feinberg has managed victim compensations for major catastrophes, including mediating resolution of Agent Orange claims and serving as special master of the September 11th Victim Compensation Fund; recently, he was hired by the Justice Department to oversee the $500 million 737 Max Victims Fund allocated for the families of those killed in the two crashes involving Boeing 737s.

Mr. Feinberg is also an adjunct professor of law at Georgetown University Law Center, the University of Pennsylvania Law School, Columbia University Law School, New York University Law School, and the University of Virginia Law School.

This transcript of a phone interview has been edited for accuracy and clarity.[2]

Transcript

YPFS: **In an interview, you referred to the fact that a large sum of guaranteed cash was immediately available to executives as "the perfect storm" when it came to executive compensations. Why did so many companies**

[1] The opinions expressed during this interview are those of Mr. Feinberg, and not those any of the institutions with which the interview subject is affiliated.
[2] A stylized summary of the key observations and insights gleaned from this interview with Mr. Feinberg is available in the Yale Program on Financial Stability's *Journal of Financial Crises*.

struggle to find a balance between cash, stock, and other payment methods?

Feinberg: There were two reasons. First, the politics of the Troubled Assets Relief Program [TARP]. When you provide massive taxpayer money to assist companies so that they can survive, the idea that on a parallel track these companies were providing huge amounts of immediate cash compensation to executives caused a real political firestorm in the Congress. Secondly, at a time of great financial uncertainty, the idea that executives were protected from the fluctuations of the marketplace by hard cash was also a convenient way for executives to balance cash, stock, and other payments by getting the bulk of their compensation in cash and not having to worry about the fluctuations in the marketplace when it came to stock. So, it really did pose a public concern about private compensation.

YPFS: Why were the structures to ensure executives had skin in the game not established before?

Feinberg: You will have to ask [that question to] each company. It is very difficult to answer a question like that across the board, but I think that the reason there was not more skin in the game is because in the competitive private marketplace, maintaining executive loyalty to a company required immediate financial gratification, not long-term success. That was part of the problem here.

YPFS: While you were establishing the TARP executive compensation program, there were criticisms that the companies, which had their executives' compensation restructured, would be affected negatively because they would lose their top talent. It seems like there was a very delicate balance between the public's interest in how government money is spent and making sure these companies did not lose the top talent that they needed to be successful. How did you balance those two interests when restructuring executive compensation?

Feinberg: First of all, I never agreed with the premise that if you do not maintain favorable executive compensation principles, executives would leave the company and the company would then become competitively disadvantaged. I never believed it, it was never demonstrated that would be the case, and it did not turn out to be the case. What I did try and do, during my tenure at the Treasury Department, was to come up with a balanced compensation formula, a balanced structure that would maintain executive loyalty within reason, while at the same time, tie that loyalty and that executive's ultimate compensation to long-term, not short-term, company growth as reflected in stocks and other forms of compensation.

YPFS: **What resources did you consult? There was communication with the companies and market research on how executives in similar companies were compensated. It seems like hard work.**

Feinberg: It wasn't particularly difficult. The principles were spelled out in the statute creating the Treasury oversight, which I was in charge of. It was basically largely common sense that you tie executive compensation not only to the cash generated short-term by the company, but to long-term stock in the company, so that as the stock increases in value, executive compensation increases in value. As stock drops long-term, overall executive compensation is diminished. The real goal of the program was to, in a more convincing fashion, tie the total compensation package offered to executives to the longer-term performance of the company, and that is what we did. Of course, we did other things such as preventing officials from joining country clubs or taking private planes while the company was still dependent on public taxpayer support. However, generally, the key to the program was better aligning executive compensation to longer-term company performance.

YPFS: **You mentioned certain principles that you relied on in determining the executive compensation structures. Can they be applied to the determination of executive compensation in all crises, including the one we are going through? Can they be applied to companies during periods of relative economic stability?**

Feinberg: These principles were determined by the statute passed by Congress; I did not make up these principles. I was required to factor in principles like risk, taxpayer return, allocation between cash and stock, short-term growth vs. long-term growth, etc. All of that was spelled out in the enabling legislation enacted by Congress.[3] Now, should these principles govern in other circumstances? Well, I think they should, but that is not the federal government's role. This law creating the special master and the fact that Treasury would oversee the program was very unique to TARP. It has not been replicated, and I do not think it will be replicated. If companies on their own, privately, want to endorse these principles as governing principles to determine executive compensation, that is fine, but the statute is not much of a precedent in mandating these changes among private companies.

YPFS: **In your 2010 report[4], you propose a "break policy" for TARP recipients, so that their compensation committee can restructure, reduce, or cancel**

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[3] Details regarding the principles applicable to executive under TARP can be found at the Treasury's webpage: Executive Compensation Rules and Guidance | US Department of the Treasury – https://home.treasury.gov/data/troubled-assets-relief-program/executive-comp/executive-compensation-rules-and-guidance

[4] Available at https://home.treasury.gov/sites/default/files/initiatives/financial-stability/TARP-Programs/executive-comp/Documents/Final%20Report%20of%20Kenneth%20Feinberg%20-%20FINAL.PDF

pending payments to executives in extraordinary circumstances, such as a financial crisis. Is this like an automatic circuit breaker?

Feinberg: It is presumptively automatic. The idea is that compensation committees can pause and restructure compensation. Now, that is a potential circuit breaker. Whether or not those private compensation committees will engage is a separate question. If you ask whether this break policy has been used by companies once the federal government got out of the business of regulating compensation, my answer would be: (A) I do not know, (B) you probably will have to check company by company, as to whether the break policy and the automatic circuit breakup concept has been endorsed and implemented. I do not think you can answer "yes" or "no" to that question, you have got to look at each company and how it deals with midcourse corrections and compensation.

YPFS: You conclude at the end of the report that it would be inappropriate and impractical to replicate the program across a larger number of firms. What was the reason behind that conclusion?

Feinberg: The federal government should not be in the business of regulating private corporate compensation. I do not think the Founding Fathers or policy makers today think that it is wise or beneficial for this strong arm of the federal government and the Department of the Treasury to impose its principles and its scriptures on private compensation and private companies.

TARP was unique. It was a unique financial crisis in American history. The Congress, having decided to bail out Bank of America, or Chrysler, or General Motors, or Citibank, or AIG, felt, "Alright, we have provided taxpayer assistance; we are now public creditors of those companies. We have loaned them money which has to be repaid; we also, as public creditors, should have a say in executive compensation." Those companies paid back the Treasury with interest; they then escaped the oversight of the Department of the Treasury. I do not think that the program that I administered is likely to be replicated, or expanded, because I do not think that is the appropriate role of the federal government when it comes to the free marketplace and private compensation.

YPFS: Do you think that inappropriate compensation structures can pose a risk to our financial system?

Feinberg: Sure. It did in 2008, 2009; it could happen again. The answer lies in how you deal with that risk. The answer to that is, within American history, it has always been dealt through the free market; that is market midcourse correction, private midcourse correction. Occasionally the federal government, in whole or in part, engages in compensation structures. The

Federal Reserve governing banks, the Federal Home Loan Bank Board… There may be, at the edges, some regulatory interference, but it is modest. The notion of replicating the statute that I administered, which was not at the margins but was a heavy federal government Treasury Department intervention, is unique. Therefore, I believe that although compensation structures can pose a risk, it is the marketplace that tries to correct them.

YPFS: **Have there been any improvements in the way companies structure their executive compensation since the Global Financial Crisis?**

Feinberg: I am dubious. I tend to doubt that there have been any major structural changes in compensation. As I said before, I think my year's tenure at the Treasury was largely a sideshow and that it was a political response to heavy, heavy taxpayer intervention through loans. I do not see that there has been much of a shift. Research has been done since TARP, and I do not think there has been a whole lot of change in the program, in private compensation mechanisms.

YPFS: **During the 2007–2009 crisis, the government's efforts were usually seen as helping Wall Street and neglecting Main Street. Your work, especially with the executive compensation, at that time was unique in the sense that it made Main Street really happy; it got a lot of support from them, and—you even joked about it—it did not make Wall Street happy at all. Do you feel measures such as this could contribute to social peace and therefore to the reduction of systemic risk?**

Feinberg: No. I think that one who looks at curbing executive compensation as a measure that will somehow promote social peace and narrow differences equitably between Wall Street and Main Street is expecting way too much from a program like the one I administered. Now, having said that, I do believe that paying more attention to narrowing the gap between Wall Street and Main Street by providing social and financial incentives to improve Main Street compensation and Main Street economic security, as it is done in a major way in the current 2021 COVID relief legislation, is important. I do not think that curbing private compensation through public intervention is going to be an effective tool to narrow those differences and to promote social peace. I think promoting social peace by narrowing the inequity between Wall Street and Main Street is important in and of itself.

YPFS: **What are the lessons we can draw from the crisis of 2007–2009?**

Feinberg: The lesson is clear as day: The government, the Congress, and federal regulators, went way too far in freeing up private companies from financial and economic regulation. Deregulation efforts, starting with the Reagan Administration in the 1980s, and including deregulation on the part of Democratic and Republican administrations, went beyond appropriate limits.

Relying on the private marketplace to regulate itself, to the extent that deregulation created a regulatory vacuum, was a major mistake. Senator Dodd and others' efforts in trying to at least impose some regulatory restraints on the private marketplace were a step in the right direction. Dodd-Frank, for example did not go far enough, could not probably get political support to go further. But I think that regulation of the financial marketplace and the absence of that regulation is a major issue even today. The other lesson, of course, is the lesson I have already articulated: Do not count on the private marketplace to regulate itself.

YPFS: Do you think that can be achieved?

Feinberg: Well, if you are asking me if I think there can be some further regulatory interference from the federal government, if you have got that type of political leadership in the White House or the Congress, [the answer is] yes, I think there are chances you can do that. Is it likely? It is a challenge. The free market, proponents of the free market, having won the battle 40 years ago to deregulate financial institution oversight will not easily give up that freedom, but it is an important aspect of all of this.

YPFS: Do you see any opportunities in terms of improving compensation structures during this current crisis?

Feinberg: Again, it is not a role for the federal government to interfere to that extent. Therefore, I am not sure you will see much improvement. I have not seen it other than those mandated improvements that I promoted during the brief tenure of the law, but that law has not been expanded, it should not be, and I am dubious that we have seen or will see any type of opportunity to really improve the structures.

YPFS: What systemic risks do you see at the moment?

Feinberg: They are the same. To what extent are financial institutions so big that they are too big to fail? To what extent [should we be] allowing the private market to competitively determine compensation structures? To what extent is risk creation still a priority in the private marketplace? Short-term gain rather than long-term security, all of these issues were made, and the regulators in the Congress must be ever vigilant. It might be the price one pays for capitalism in the free markets. On the other hand, to what extent should the Federal Reserve, the Congress, the Federal Home Loan Bank Board, [the Office of] the Comptroller of the Currency, et cetera, be reinvigorated by existing institutions to try and do something? That is the question.

YPFS: When we were talking about Main Street and Wall Street, you mentioned that there can be some social and financial incentives for Main Street to improve its economic situation. Do you have anything in mind that we can do?

Feinberg: Well, as we have seen it in the law enacted by Congress and signed by President Biden, you can narrow the inequities of compensation, or the financial inequities between corporate compensation and Main Street through the Child Tax Credit, through incentives, through expanded unionization, through employment benefits, etc. But it is important to distinguish between the compensation of Wall Street executives versus Main Street executives, or mainstream workers. Compensation is a relatively narrow issue. If you are looking at ways to narrow the inequity between overall financial benefit to corporate executives and Wall Street and the working man on Main Street, that is macroeconomics; that is a whole other issue.

How do you narrow the gap between the high end and the low end in American society? That is a huge problem, way beyond compensation. The recent enactment of the legislation providing huge amounts to preserve pension plans, for example, for workers on Main Street, to try to bring childhood poverty under control, etc. I think that is a much bigger task and a much bigger assignment than just focusing on compensation.

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