

EXECUTIVE BONUSES CLAWBACK: THE WORLD'S LARGEST BANKS CASES

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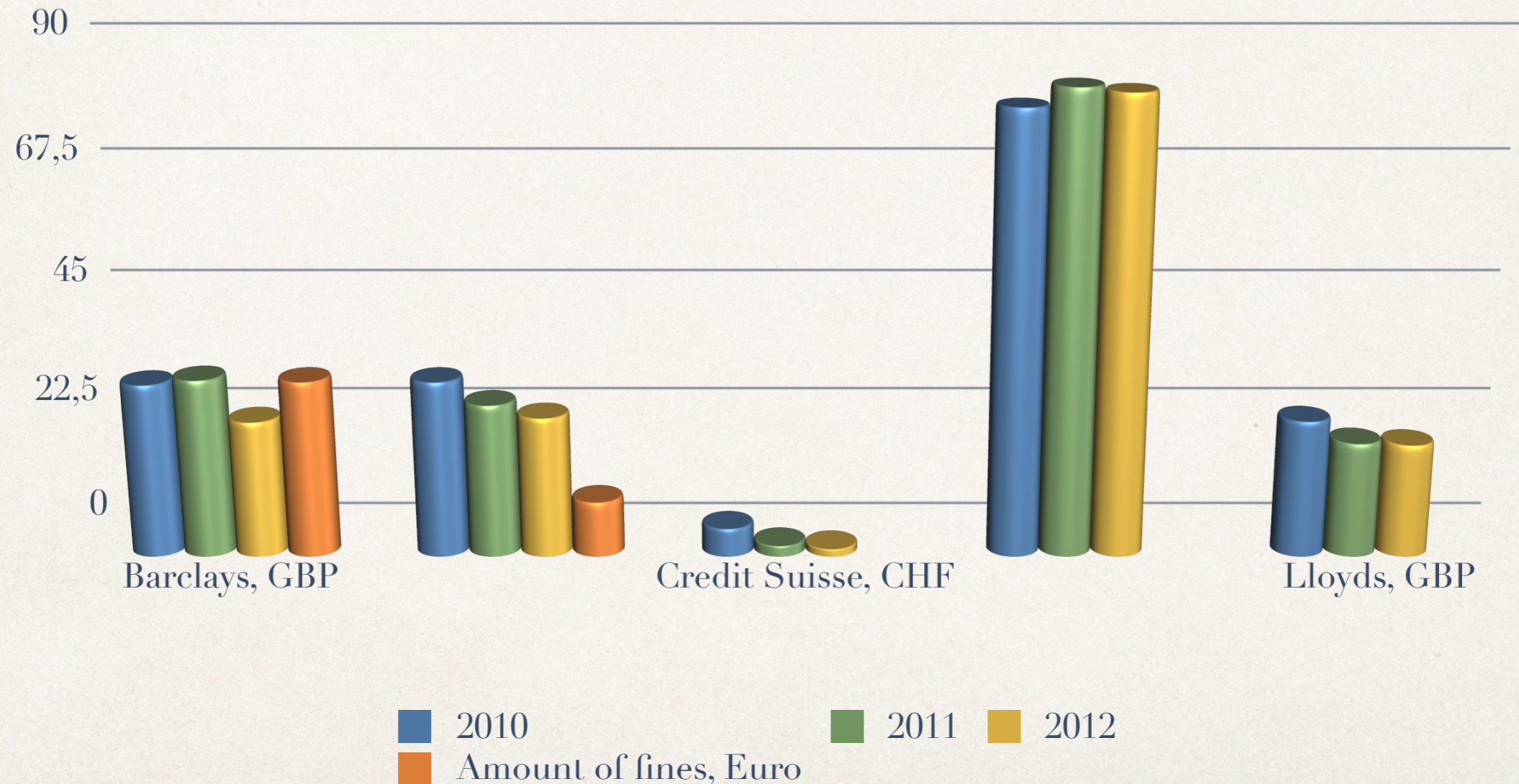
“The salary of the chief executive of a large corporation is *not a market award for achievement*. It is frequently in the nature of a warm personal gesture *by the individual to himself*”

– *John Kenneth Galbraith, American economist*

Ratio of Variable-to-Fixed Remuneration for selected EU banks' CEOs in 2006-2011

Bank	2006	2007	2008	2009	2010	2011
Barclays	2.6	3.3	0.0	0.0	2.5	3.7
Credit Suisse	n/a	n/a	0.0	0.0	4.1	1.33
Deutsche Bank	10.4	11.0	0.0	7.2	2.8	2.8
HSBC	1.6	0.9	0.0	3.7	2.4	3.6
ING Bank	3.1	2.7	0.0	0.0	0.9	0.0
Royal Bank of Scotland	6.3	6.7	5.2	4.4	5.1	5.4
Standard Chartered	1.9	3.6	2.9	3.7	4.0	3.7
UniCredit	n/a	n/a	n/a	0.2	0.5	0.0

Total income and regulatory fines (due to LIBOR scandal) of selected European banks in 2010-2012, mln.



“Clawback is contractual agreement in which the staff member agrees to return ownership of an amount of remuneration to the institution under certain circumstances”

– *Committee of European Banking Supervisors, Guidelines on Remuneration Policies and Practices*

Guidelines and recommendations on bonuses clawback:

- ❖ *Guidelines on Remuneration Policies and Practices* (Committee of European Banking Supervisors, 2010) directed to national regulators of EU countries
- ❖ *FSF Principles for Sound Compensation Practices* (the Group of Twenty, 2009)
- ❖ *Financial Services Authority (FSA) Remuneration Code of UK* (2010)
- ❖ *FINMA Circular* (Switzerland, 2009)
- ❖ Regulator of financial institutions Bafin in Germany (2009)

Executives' bonus clawback was firstly introduced by UBS

The bonuses' deferral period was prolonged from 3 to 5 years.

The amount of award that could be clawbacked in case of not achieving the average adjusted pre-tax profit during the period by the bank is equal to 100%.

If RoTE level is less than 6%, the bonus can be forfeiture partially or to full extent.



Executive directors' compensation mechanism (including CEO) in UBS

Current year	Equity ownership plan (EOP) 40%	Deferred Contingent Capital Plan (DCCP) 40%	Cash 20%	Base salary
1 st year			20%	
2 nd year				
3 ^d year	14%	Shares awarded. Up to 100% can be forfeited	Awards in the form of notional bonds. Awards are subject to 20% forfeiture	
4 th year	13%			
5 th year	13%			40%

Structure of bank executives' bonuses subjected to clawing back

Criterion		UBS	Barclays	Credit Suisse	Deutsche Bank	HSBC
Structure of award's deferred part	Cash	-	+	+	+	-
	Shares	+	+	+	+	+
Subjected to clawback		About 80% of deferred bonuses	All deferred bonuses	Short-term part of deferred bonuses	All deferred bonuses	All or part of award

The differences of executive bonuses clawing back among banks are in:

- ❖ Covered employees (CEO; CEO, CFO; all executive officers)
- ❖ Covered compensation (cash; equity; all)
- ❖ Triggering events

Three categories of triggering events:

❖ Performance-based

- *Royal Bank of Scotland,
Lloyds*

❖ Fraud-based

❖ Both

- *Barclays, Credit
Suisse, Deutsche Bank,
HSBC, UBS*

Example: HSBC

Triggering events for bonuses clawback:

1. Financial measures:

- capital strength on the base of Core Tier 1 capital ratio, return on equity, cost efficiency ratio
- dividend payout

2. **Non-financial measures** are estimated with the aim to define the necessity of award clawback include successful execution of strategy and measures related to risk and compliance.



Summary of executive bonuses' clawing back in individual European banks in 2010-2012

Bank	Year	Executives subjected to clawback	Clawback amount	Triggering event
Barclays	2012-2013	15 current and former employees	Clawing back £300m of unvested deferred and long term incentive awards	LIBOR investigation and other risk issues in 2012
HSBC	2012	Former chief executive former -head of the Mexican unit	£2m of unvested shares	Mis-selling of nearly £300m of long-term care bonds to elderly customers
Lloyds Banking Group	2013	Former chief executive and 12 former directors	- 80% of CEO deferred award - 40% of director's deferred award	Mis-selling of payment protection insurance in 2009
Royal Bank of	2012	Two executive directors	£112 m	Libor scandal
UBS	2011-2012	Investment bankers whose bonuses exceeded \$2 million	50% of share-based bonuses awarded. Approximately CHF 60 million of unvested deferred performance awards has been forfeited	Libor scandal (according to regulatory demand to pay \$1.5 billion in fines)

Clawback provisions: the case of American banks

- ❖ 2002 - **Sarbanes-Oxley Act (SOX)** which gave the right to Securities Exchange Commission to forfeiture the executive remuneration in case of misconduct
- ❖ During the global financial crisis 2008-2009 in banks that have got the financial assistance from **TARP** chief executives' remuneration included clawback provisions
- ❖ 2010 – in the Dodd-Frank Act the requirement to exchange-listed firms has been included: in case of financial misstatement the compensation has to be forfeited from the executives over three-year period before the date of misstatement accounting

US peculiarities on clawback provisions vs. UK:


- ❖ applies to all executive officers, but not only to CEO and CFO
- ❖ the act of “misconduct” is not required
- ❖ the term of incentive-based parts of compensation restricted to clawback is prolonged: from one-year to three-year period. But still it is less than five-year term of clawing back possibility according to FSA Remuneration Code

Conclusions (1)

- ❖ Different character of bonuses clawback provision



Moderate forfeiture clauses (Deutsche Bank, HSBC, Credit Swiss)



Stricter forfeiture clauses (Lloyds Banking Group, Royal Bank of Scotland)

Conclusions (2)

- More *concentrated* ownership structure
- Prevailing *state* ownership



Stricter provisions of bonus clawback for senior executives

❖ Example:

Government's share in **Lloyds** and **Royal Bank of Scotland** equals to 32.7 and 65% respectively.

These banks have been among the first that have implemented clawback clauses

In contrast:

- ❖ in **Deutsche Bank** the only large shareholder (*BlackRock Inc., New York*) holds 5.14% of bank's shares
- ❖ in **Credit Suisse**: less than 10 large shareholders own more than 3% (the maximum stake equals 6.7% (*Olayan Group*))

Conclusions (3)

- Market concentration in
the banking sector



Stricter provisions
of bonus clawback
for senior
executives

Country	HHI*	Top 5 banks'
Switzerland	787.5	56.4 %
UK	601	59%
<i>In contrast to:</i>		
Germany	275	29.5%

**Deutsche Bank Markets Research, "European Banks Strategy" (2012)*

Thank you for attention.