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THE IMPACT OF THE FINANCIAL CRISIS ON THE REGULATIONS OF MANAGERIAL STAFF REMUNERATION IN FINANCIAL INSTITUTIONS

1. REMUNERATION REGULATIONS IN THE FINANCIAL SECTOR BEFORE THE CRISIS

Regulation and supervision of the banking sector in the modern economy is a standard that has been formed for many decades. Its purpose is to maintain security, which can be simply defined as a desire to minimize the number of bankruptcies in the banking sector (Iwanicz-Drozdowska, 2012). Regulations regarding banks are based on the assumption of market imperfection, the existence of externalities, associated with bank insolvency or banking crises and information asymmetry (Miklaszewska, 2004). The United States was an example of a country with very strict regulations introduced concerning the principles of managerial remuneration. The provisions referring to public companies subject to the regulations of the Securities Exchange Commission have been included in the *Code of Federal Regulations, Regulation SK* (Urbanek, 2010). This regulation describes in detail how the structure of managerial staff remuneration in every public company should be presented. The remuneration committee should be appointed as part of the company, which is required to annually provide a report to shareholders on the principles of remuneration of the key managers in the

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company. The company is required to disclose the detailed remuneration of the CEO and at least four main managers of the company. In companies there is no obligation to publish the remuneration of individuals who in a given financial year received a remuneration lower than 100 000 USD (*Code of...*, 2003).

Before the financial crisis of 2007–2009, the European Union regulated remunerations in a single directive (Directive 2001/34/EC) and two particular recommendations (Commission recommendations 2004/913/EC, 2005/162/EC). The directive of the European Parliament in 2001 (2001/34/EC) had a considerable impact on the regulations regarding publication of the amount and structure of managerial staff remuneration in companies listed on the stock exchange. The directive stated that the remuneration paid and benefits in any form granted during the last completed financial year and included in the fixed costs or paid as part of the retained earnings to the members of the administrative body, management and supervisory bodies representing in total the total amounts – must be indicated in the financial statement.

In 2004 the European Commission issued a recommendation (2004/913/EC), which became the basis for regulation of managerial staff remuneration in the European Union. In the recommendation of the European Commission, the information concerning remuneration can be divided into three parts: the remuneration policy, the remuneration of particular directors and remuneration based on shares. The most important issues relating to the remuneration policy in this recommendation were focused on:

- ❖ disclosure of the remuneration policy pursued by directors in the annual financial statement or in the notes to the annual financial statements of the company and on the website of a company listed on the stock exchange,
- ❖ document disclosing the remuneration policy should contain specific information about the relationship between work productivity and remuneration, explanation concerning the annual bonus scheme and other non-cash benefits, information on the duration of contracts with executive directors, the applicable notice periods and severance payment provisions for termination of the contract.

The global financial crisis has changed the situation of banks in the global financial market and has identified the need for fundamental changes in both regulatory systems and strategies of the banks themselves (Miklaszewska, 2010). In response to the financial crisis, the regulators have proposed a modification or a major change of the existing legal solutions intended for e.g. increasing the sense of security among the customers of financial institutions (Zaleska, 2010).

In October 2008, the president of the European Commission – J.M. Barroso, entrusted the function of directing a group of notable specialists in the field of finance to Jacques de Larosiere – former president of the European Bank for Reconstruction and Development. This team was appointed to prepare a report

presenting the essential proposals and recommendations on the future regulations of the financial market and financial supervision in Europe (Kasiewicz et al., 2013). The final document was published on 25 February 2009 (De Larosiere report, 2009). The report included 31 recommendations, one of which concerns the managerial staff remuneration in financial institutions:

– recommendation 11: in the light of the ineffectiveness of corporate order exposed by the current financial crisis, the group is of the opinion that the motivation system by remuneration should in greater amount include the interests of the partners and the shareholders and the profitability of the whole enterprise in the long term. For this purpose, the structure of the remuneration scheme in the financial sector should be based on the following rules; when specifying the amount of the premium, the long-term time horizon should be taken into account, and the payment of premiums should be spread over the entire business cycle. The same rules should relate to entities performing operations on their own account and entities managing the assets. The premiums should reflect the actual achievements and should not be guaranteed in advance. The supervisory authorities should control whether the remuneration policy in the financial institutions is suitable, request for its correction if it encourages taking excessive risk, and – if necessary – impose additional capital requirements on the basis of the second pillar of Basel II regulation, when the proper corrective actions have not been taken.

In April 2009, in response to the financial crisis, the European Commission issued two recommendations on remuneration in the financial services sector (Commission recommendations 2009/384/EC, 2009/385/EC). In the recommendation on the remuneration of directors of listed companies on the regulated market, the main aim was to ensure transparency of practices in the area of remuneration. The cause of the necessity to implement this recommendation was a change in the structure of remunerations, which under the influence of the financial crisis underwent a further-reaching complication and excessive connection with short-term results. The recommendation proposes that:

- ❖ the structure of the remuneration of directors favour the long-term stability of the company,
- ❖ it is necessary to guarantee that the severance payment does not constitute a reward for failure,
- ❖ the systems of remuneration of directors with shares, should be more closely related to the results of the company.

These recommendations are an important direction of the changes that were set by the European Commission before the managerial staff in listed companies. However, these recommendations were only an outline of the changes that should be made, simultaneously not providing specific solutions in the field of remunerations.

2. EUROPEAN UNION POST-CRISIS REGULATIONS OF MANAGERIAL STAFF REMUNERATION IN BANKS

The situation in the European financial market in 2009, as well as discussions on the level and structure of managerial staff remuneration in banks, led to work on the EU directive within the regulation of remuneration in financial institutions. In June 2010, the European Commission published a so-called green paper (Green paper 2010). In this document, the EC referred to the de Larosier report, pointing to the need for regulation in order to prevent possible irregularities in the system of corporate order in the banking sector. The management of financial institutions has been subjected to criticism in the green paper. This organ has been criticized mainly for the following:

- ❖ lack of sufficient diversity of the management board composition. This lack resulted from the omission of gender balance, social background, cultural affiliation and education of the members,
- ❖ lack of profound analysis of the management board as a whole and its individual members,
- ❖ boards were unable or unwilling to watch over the appropriate frames of risk management.

In the Green Paper it was suggested that a new category of shareholders be created. They show little interest in the long-term objectives of corporate order in enterprises/financial institutions in which they invest, and they can encourage excessive risk-taking due to the fact that their investment horizon is relatively short (3 months or half a year) (Khuran, Zelleke, 2009). The European Commission has started a debate on excessive remuneration, where as a basis for discussion two statements were taken:

- ❖ a significant increase in the variable component of the managerial staff remuneration in companies listed on the stock exchange, which took place from the end of the eighties, raises the question as to the detailed rules for the content of management activities assessment,
- ❖ remuneration policy in the financial sector based on short-term profits, without considering the associated risk contributed to the financial crisis.

The impact of the financial crisis on managerial staff remuneration played a key role in the shape of a directive regulating remuneration policy in financial institutions. The most important reason for the creation of the directive was tackling the inconsiderate and excessive risk in the banking sector, which was mainly due to the inadequate remuneration structure of some financial institutions. Remuneration policy encouraged to take on risk that exceeds the general level of risk tolerated by the institutions (Directive 2010/76/EC). The subjective scope to which this directive relates contains at least:

- ❖ senior management,

- ❖ persons making decisions about risk,
- ❖ staff dealing with control,
- ❖ any employee whose total remuneration, including unspecified pension benefits is at the same level of salary scale as the remuneration of senior management and persons making decisions about risk.

The main purpose of the regulation was to indicate clear rules concerning the correct system of remuneration intended to ensure that the structure of remuneration does not encourage individuals to take excessive risk. Total remuneration should not constitute a moral hazard and must be related to the risk taken by the financial institution. The main changes that entail the adjustment can be divided into three parts; provisions regarding not complying with the guidelines, information requirements related to financial institutions and regulations concerning variable remuneration. Failure to adjust to the guidelines involves a number of consequences. National authorities may impose financial or non-financial penalties, in the situation of not having a remuneration policy which is consistent with the guidelines. In the financial institution which does not fulfil the provisions of the directive, it may be necessary to limit the variable remuneration to a percentage of total net income.

Numerous information obligations have been imposed on financial institutions. The proper national authorities need to gather information about individuals whose earnings exceed 1 million EUR. Banks must at least once a year announce: the composition and scope of function of the remuneration committee, the major parameters and justification of any kind of variable remuneration systems, quantitative information on remuneration (including remuneration for the given year) – divided into fixed and variable remuneration, the amount and form of variable remuneration (including cash, shares and share-linked instruments), the amount of deferred remuneration – divided into parts already eligible and not eligible, and the amount of payments connected with the termination of employment contracts. The most significant and extensive changes are connected with variable components of remuneration. Guaranteeing variable remuneration is not possible. Apart from one exception, which is guaranteeing variable remuneration in the first year of work, but this should be used only in exceptional situations. A substantial part of the variable remuneration payment – 40–60%, should be spread over a period of not less than 3 to 5 years. A large part of any variable remuneration exceeding 50% should be composed of shares or corresponding property rights of the financial institution. There is a possibility of reducing the variable remuneration in the situation where the financial institution gets weaker or yields negative financial results. This concerns both the current premiums and reductions in payouts of amounts previously earned, among others by reduction of remuneration (malus) or clawback of a previously paid premium (clawback).

Introduced provisions were supervised by the European Banking Authority. In issued reports (EBA, 2011) concerning the amount of wages in the financial

institutions of the EU, a specific description of the level and structure of managerial staff remuneration was presented. The number of people employed in the financial sector with high incomes – more than 1 million EUR per year is presented in Table 1. Of all the EU countries, only two did not disclose the information about the number and level of remuneration in the year 2010, one in 2011, whereas all countries revealed this information in 2012. In 2011, only Poland did not release this information.

Table 1. The number of people employed in financial institutions of the EU receiving an annual remuneration of more than 1 million EUR

Member States	2010	2011	2012
Austria	14	10	19
Belgium	13	8	15
Bulgaria	0	0	0
Cyprus	3	4	3
Czech Republic	0	0	0
Denmark	29	33	48
Estonia	0	0	0
Finland	5	3	6
France	292	162	177
Germany	195	170	212
Greece	0	2	1
Hungary	1	8	9
Ireland	21	21	17
Italy	119	96	109
Latvia	0	0	0
Lithuania	0	0	0
Luxembourg	6	10	15
Malta	0	0	0
Netherlands	43	36	27
Poland	2	4	7
Portugal	13	11	6
Romania	1	0	1
Slovakia	1	2	1
Slovenia	0	0	0
Spain	133	125	100
Sweden	14	15	20
United Kingdom	2525	2436	2714
UE 27	3430	3156	3507

Source: own presentation, based on: EBA Report High Earners 2010, 2011 and 2012.

The largest number of people who are rewarded for their work in financial institutions with over 1 million EUR per year, is in the UK. In this country, the number of people rewarded with over 1 million EUR constituted 77% of all persons rewarded with more than this amount all over the European Union. Among the 27 EU countries, in seven countries in the years 2010–2012 there was not a single person who earned over 1 million EUR in a financial institution. It is worth noting that Poland in 2010–2011, and Hungary in 2010, did not reveal the list of persons rewarded with more than 1 million EUR in financial institutions. The data presented in the table indicates the amount reported by other EU countries, which have subsidiaries in these countries. Table 2 shows fixed and variable remuneration that was received by all persons rewarded with over 1 million EUR, employed in financial institutions. In the years 2010–2012, variable remuneration received by the staff rewarded by financial institutions in the EU, was on a much higher level than the fixed remuneration obtained by these people. In 2010, it was a difference of 5 billion EUR in 2011 2.3 billion EUR, and in 2012 3.4 billion EUR.

Table 2. Fixed and variable remuneration of people rewarded in financial institutions with over 1 million EUR (in million EUR)

Fixed remuneration	2010	2011	2012	Variable remuneration	2010	2011	2012
Austria	12	10	19	Austria	11	9	16
Belgium	8	5	8	Belgium	10	6	11
Bulgaria	0	0	0	Bulgaria	0	0	0
Cyprus	2	4	3	Cyprus	1	3	3
Czech Republic	0	0	0	Czech Republic	0	0	0
Denmark	17	30	37	Denmark	26	19	33
Estonia	0	0	0	Estonia	0	0	0
Finland	3	1	3	Finland	3	2	4
France	73	54	58	France	449	203	219
Germany	85	86	106	Germany	298	226	224
Greece	0	2	0	Greece	0	2	1
Hungary	0	3	4	Hungary	1	9	11
Ireland	8	7	7	Ireland	24	22	17
Italy	94	83	80	Italy	154	75	100
Latvia	0	0	0	Latvia	0	0	0
Lithuania	0	0	0	Lithuania	0	0	0
Luxembourg	3	7	8	Luxembourg	8	10	16

Fixed remuneration	2010	2011	2012	Variable remuneration	2010	2011	2012
Malta	0	0	0	Malta	0	0	0
Netherlands	24	23	23	Netherlands	49	30	17
Poland	1	2	4	Poland	2	5	10
Portugal	6	5	5	Portugal	13	13	3
Romania	1	0	1	Romania	0	0	0
Slovakia	1	0	0	Slovakia	0	3	1
Slovenia	0	0	0	Slovenia	0	0	0
Spain	91	107	91	Spain	209	198	126
Sweden	8	14	16	Sweden	8	8	13
United Kingdom	817	784	1127	United Kingdom	5000	2718	4169
UE 27	1255	1226	1601	UE 27	6265	3561	4995

Source: own presentation, based on: EBA Report High Earners 2010, 2011 and 2012.

Swiss society in early 2013 stated that it is important to introduce the regulation of remunerations in the Swiss financial system. Swiss law is constructed in such a way that in fact citizens make decisions on important issues connected with the functioning of their country. In Switzerland, every three months, a nationwide referendum is held in which citizens opt for settling two to five essential cases. What is the most important: the decisions of the population are binding to the Swiss parliament. In order to discuss a given project in a referendum from the initiative of citizens, it is necessary to collect 100 000 signatures within 18 months. In February 2013, Swiss citizens voted in a referendum on a draft concerning limiting the remunerations of Swiss managerial staff. Nearly 70% of the population was in favour of limiting the salary of managerial staff. The introduced changes are set to revolutionize the amount of remuneration of managerial staff. The draft indicated that:

- ❖ the shareholders at the general meeting will vote on the remuneration of board members and supervisory board – voting will be binding and will be possible to be held electronically,
- ❖ a general meeting of shareholders each year will decide on the composition of the supervisory board, including its chairman and the composition of the committee for remuneration,
- ❖ the practice of representation at the general meeting of institutional shareholders by the board of directors is prohibited,
- ❖ severance payment, advance payment and premiums for the purchase and sale of companies are prohibited,

- ❖ not complying with the implemented law is to be punished with imprisonment – up to three years, and a financial penalty – up to six annual salaries.

At the end of 2012, the European Banking Authority issued guidelines on the assessment of the qualifications of the management body members and the people performing the most important functions (EBA, 2012). The document specified the criteria and processes to be followed by financial institutions in assessing the qualifications of the proposed and appointed members of the financial institution management body performing both a managing and supervisory function. The guidelines suggested that each institution had a policy of selection and assessment of management body members, which should contain, at least:

- ❖ the person or unit responsible for making the assessment of qualifications,
- ❖ the relevant internal procedure for the assessment of member qualifications,
- ❖ the competences and skills of the management body member necessary to presume that a member has sufficient expertise,
- ❖ information and evidence that a member of the management body should present to the credit institution to assess,
- ❖ if a member is to be appointed by the shareholders, the measures taken to ensure that the shareholders were informed of the requirements regarding the position and profile of the candidates before their appointment,
- ❖ situations in which it is necessary to reassess the qualifications, along with measures to identify such a situation,
- ❖ ways of providing opportunities for training by the institution in the case of specific training and development needs of the management body members.

The criteria for assessing the member of the management body according to the guidelines of EBA are divided into three parts: criteria relating to reputation, criteria connected with experience and criteria for management. The essential issue in the criteria relating to reputation is good repute. The guidelines were issued to pay special attention to factors that may question the good repute of a member such as; judgment or prosecution of a criminal offence, significant current or future investigations to enforce the law in relation to a member, or the imposition of administrative sanctions for failure to comply with all provisions regarding financial activity. The criterion connected with experience pays specific attention to the educational profile of the management body member. Education related to banking and financial services, is considered as education in the field of banking and finance, economics, law and administration of financial regulations and quantitative methods. The management body member, apart from a theoretical education, should have practical education, where important are the following: the period of holding their position, the range of competences, decision-making authority and responsibilities, the number of subordinates and technical knowledge acquired in the position concerning the activity of the credit institution and understanding risk in the activity of credit institutions. The criteria for

management place particular emphasis on personal, professional or other economic relationships with the members of the management body and shareholders having a controlling packet. All EBA guidelines should be implemented by the competent authorities and institutions by 22 May 2013.

The European Union, from the beginning of 2013, has worked on tightening the provisions of managerial staff remuneration. It proposed that from January 2014 the maximum premium level – calculated as a percentage of the basic remuneration – be implemented. Presently, the bonus is an average of about 140% of the basic salary in European banks. The European Union has proposed limiting premium to 100% of remuneration in the form of annual salary. Nevertheless, it will be possible to raise the percentage limit to the level of 200% with the approval of shareholders. The United Kingdom was against such restrictions, but British finance minister George Osborne at this stage could not do anything because ECOFIN makes the decisions through majority vote. G. Osborne has already announced that it “would be silly” to oppose the regulation. The mayor of London Boris Johnson called the cuts “the silliest thing Europe has seen since the days of Diocletian, who wanted to regulate the prices of vegetables”. No wonder he thinks so – bonuses in London city are at a very high level. Barclays intends this year to spend 800 million pounds from its profit on a dividend. The regulation will not affect all employees of banks, but senior managers and risk takers, including traders. The regulation will affect from 300 to 500 workers in each big bank, in London alone it will be 5000 people, depending on how the definition of risk taker will be clarified. The law must still be approved by national governments and voted on during the 15–18 April session, but it is believed to be just a formality. The law would enter into force at the beginning of 2014. The consensus is a great victory of the European Parliament, which subordinated the support for the CRD IV directive to cuts in bonuses. This directive is a milestone in the regulation of the financial sector, as it implements the establishing of a Basel III compromise (*UE: Dyrektywa...*, 2013). The discussions shaping the text of the directive, having a significant impact on the level of managerial staff remuneration in banks, were completed in June 2013. On 26 June 2013 a directive was announced on the conditions of admission of credit institutions to conducting business activity and the prudential supervision of credit institutions and investment firms (Directive 2013/36/EC), and the regulation on prudential requirements for credit institutions and investment firms (Corrigendum to Regulation (EU) No 575/2013).

These documents signalled numerous obligations that should be fulfilled by institutions covered by this directive and regulation. Changes concerning the remuneration policy in the financial institutions have been described in articles 92–95 of the directive. The remuneration policy has been specifically associated with the risk of business as well as strategy and long-term objectives of the institution. The conducted remuneration policy should be verified at least once a year. The

European Union has placed a strong emphasis on reporting and transparency in publishing information concerning remunerations. It was highlighted that remuneration policy should be published with a clear separation into at least two components of remuneration:

- ❖ basic fixed remuneration – which should reflect relevant professional experience and the scope of organizational responsibility anticipated in the job description as part of the terms of employment,
- ❖ variable remuneration – which should reflect results that have been balanced and adjusted to risk, and also achieved results beyond the scope of the obligations expressed in the job description as part of the conditions of employment.

The directive made the variable remuneration highly conditional and significantly limited it. In determining the level of variable remuneration, the essential thing should be an assessment of the performance of the employee and the entire institution. This assessment should be carried out over several years, rather than based on short-term (annual) results. The directive emphasizes the prohibition of guaranteed variable remuneration. The most important change that has been implemented is to determine the ratio of variable remuneration in relation to fixed remuneration. The institutions determine the appropriate ratio of constant components of total remuneration in relation to variable components, keeping in mind that:

- ❖ the variable component shall not exceed 100% of the fixed component of total remuneration of each person,
- ❖ member states may implement a lower maximum percentage,
- ❖ member states may allow shareholders, owners or stockholders to approve the maximum level of the fixed component of remuneration to the variable remuneration, provided that the overall level of the variable component shall not exceed 200% of the fixed component of each person's total remuneration.

The shareholders, owners or stockholders, by raising the level of the ratio of variable remuneration in relation to the fixed remuneration to a level higher than 100%, must constitute a majority of at least 66%, provided they represent at least 50% of the shares. Variable remunerations in the form of early contract termination have also been limited. Severance payments should not reward poor performance and failures. An essential part of any variable remuneration component, constituting in each case at least 50%, should consist of shares or corresponding titles of ownership. A large part that is at least 40% of the variable remuneration component should be deferred for a period of not less than three to five years. Variable remuneration may be withdrawn at 100% or reduced if the member has participated in activities which resulted in considerable losses to the institution or did not meet the relevant standards concerning competence and reputation.

Verification of remuneration structure – an appropriate level of variable remuneration in relation to the fixed remuneration – forcing EU countries, by the

CRD IV directive, will be necessary in many financial systems of European countries. The ratio of variable remuneration in relation to fixed remuneration paid to individuals in financial institutions of more than 1 million EUR is presented in Table 3.

Table 3. The relationship of variable remuneration to fixed remuneration of persons paid more than 1 million EUR in financial institutions of the EU (in %)

Member States	2010	2011	2012
Austria	93	93	84
Belgium	131	118	143
Bulgaria	0	0	0
Cyprus	41	74	100
Czech Republic	0	0	0
Denmark	147	64	89
Estonia	0	0	0
Finland	115	136	138
France	615	373	375
Germany	350	263	211
Greece	0	75	302
Hungary	528	75	260
Ireland	299	336	235
Italy	163	90	124
Latvia	0	0	0
Lithuania	0	0	0
Luxembourg	230	158	220
Malta	0	0	0
Netherlands	202	132	76
Poland	143	277	278
Portugal	226	240	63
Romania	34	0	0
Slovakia	0	1911	571
Slovenia	0	0	0
Spain	229	185	136
Sweden	100	56	82
United Kingdom	611	346	370

Source: own presentation, based on: EBA Report High Earners 2010, 2011 and 2012.

The ratio of variable remuneration in relation to fixed remuneration which does not meet the criterion of 100%, did not meet the requirements of the CRD IV directive in at least 13 countries in 2012. It should be noted, nevertheless, that even in 8 countries individuals who are rewarded more than 1 million EUR were not identified. Therefore, this ratio is at the level required in the directive only in 6 countries. The relationship of variable remuneration to fixed remuneration, of more than 200% occurs in as many as 9 countries belonging to the European Union. The biggest challenge in meeting regulatory requirements will be based by financial institutions conducting their operations in France and the UK. In Poland, this ratio is over 270%, and what will be required from shareholders/owners is permission for the ratio of variable remuneration in relation to fixed remuneration above 100%, and a reduction in variable remuneration or increase in fixed remuneration, so that the relationship of these variables is not higher than 200%.

Examples of poor practice are presented in the guidelines on principles and practices regarding remuneration, prepared by the *European Securities and Markets Authority (Guidelines on remuneration..., 2013)*. The following were primarily considered bad practices:

- ❖ use of quantitative data as a criterion for variable remuneration assessment,
- ❖ lack of monitoring of risk assessment linked with the relation of variable remuneration with quantitative data,
- ❖ focus of the strategic objectives on trade and financial aspects, without taking into account the potential harmful actions directed towards the client.

In the ESMA guidelines the levels are highlighted leading to a conflict of interest, which is hard to manage. One of the most notorious conflicts is linking remuneration to the sale of individual products. For example, the institution pays the people engaged progressive motivation benefits for every product sold during a given quarter according to the following rules:

- ❖ achieving a goal 0 – 80% – no benefits,
- ❖ achieving a goal 81 – 90% – 50 euros for each transaction,
- ❖ achieving a goal 91 – 100% – 75 euros for each transaction,
- ❖ achieving a goal 101 – 120% – 100 euros for each transaction,
- ❖ achieving a goal > 120% – 125 euros for each transaction.

A motivation system constructed in such a way may lead to a desire to sell the largest number of products without taking into account ethical considerations.

3. POST-CRISIS REMUNERATIONS REGULATIONS IN THE UNITED STATES

Post-crisis regulations of managerial staff remunerations in the United States are based on the Dodd – Frank Act – reform of Wall Street (Dodd-Frank Act, 2010).

The act was signed by the president of the United States on July 21, 2010. This document was put into practice with the consumer protection act. The legal acts were a response to the problems of carrying out bank insolvency in the United States. The main purpose of the implemented changes was to promote financial stability by improving the transparency of financial markets and responsibility of financial institutions for their actions. Wall Street reform is described in the document in sixteen sections, which cover more than eight hundred pages. In this act, one section was devoted to remuneration of board of directors. In the definition of the members of the board of directors, it was noted that the regulation applies to all persons who sit on the board of directors.

The act changes numerous rules and customs of financial institutions. It is possible to reclaim the compensation granted to each director who is involved in a working relationship with the institution, and that of those who are not working in the institution. Any form of remuneration may be reclaimed (premiums, bonuses, severance payments, deferred remuneration, benefits and profits earned from the sale of securities). At least once every three years, each institution is required to submit to a shareholder vote the level and structure of managerial staff remuneration.

The Act emphasizes the special role of remuneration committees. The legislation stipulates that every company should have a remuneration committee and the lack of such a committee entails the necessity of informing of the reasons for this state. Each member of the committee should be independent. Establishment of an independent member profile, however, is not obvious. Independence should be determined primarily by the remuneration which a member should obtain only for advisory services. An independent member should not be linked to any other subsidiary company of the capital group. Such a person should not have any business relationships with the financial institution and the managers of this institution either. The committee should operate within the board of directors, so it is possible to obtain the advice of external consultants. Consultants and independent legal advisers should receive a remuneration that is at a fair level and reflects the market, paid within the work of the operating committee. The remuneration committee is responsible for appointing top managers, the level and structure of managerial staff remuneration and supervision of the remunerations of the board of directors.

The need for publication of the remuneration of the board of directors was reiterated along with the need for it to be transparent terms of the level and structure of said remuneration. It was also necessary to link the level of remuneration with the financial results of the company, paying special attention to the change in the value of shares and paid dividends. The need for publication of remunerations is not limited to the remunerations of the board of directors. Companies are required to publish:

- ❖ the medians of the total annual remuneration of all employees of the institution (excluding remuneration of the general director, or a person occupying an equivalent position),
- ❖ the annual amount of remuneration of the general director, or a person occupying an equivalent position,
- ❖ the ratio of the annual remuneration of the general director to the median of annual remuneration of all employees.

The company should announce (in order to disclose such information to shareholders), whether any of the staff (especially the members of the board of directors), made any purchases of financial instruments that were designed to hedge against a decline of the market value of the company. Federal regulators determine whether the persons managing the company have significant variable remuneration in the form of various financial instruments which may result in financial losses to the institution. The main regulator has the right to verify the level of remuneration which may be determined to be too high. The definition of the main regulator is described by the act through the following institutions:

- ❖ *the Board of Governors of the Federal Reserve System,*
- ❖ *the Office of the Comptroller of the Currency,*
- ❖ *the Board of Directors of the Federal Deposit Insurance Corporation,*
- ❖ *the Director of the Office of Thrift Supervision,*
- ❖ *the National Credit Union Administration Board,*
- ❖ *the Securities and Exchange Commission,*
- ❖ *the Federal Housing Finance Agency.*

Institutions with assets of less than 1 million USD are not subject to the regulations in this section.

The Wall Street reform led to the release of numerous documents, which introduced the provisions of the signed act. Some of the essential provisions include the following documents of the Securities and Exchange Commission:

- ❖ On 4 April, 2011, the Securities and Exchange Commission (SEC) issued a final agreement on the changes relating to remuneration (*Shareholder approval...*, 2011). It recommended the need for a separate shareholder vote on managerial staff remuneration of the company. It was marked, however, that the vote on the level of remuneration is not binding either for the issuer or the management of the company. Moreover, it was ordered to introduce to the document *Proxy statement* a subsection relating to the financial instruments held by the management, which in the case of mergers, acquisitions or consolidations may affect the investment decisions of the company. The disclosure should relate to remuneration for possible dismissal to all members of the board of directors. Such information should include data on the amount of remuneration, the structure and terms of acquisition of the rights to individual components of

the remuneration. The results of non-binding votes should also be published in the annual statement of the company.

- ❖ On 20 June, 2012, the SEC issued amended rules for the disclosure of information in the *proxy statement (Listing Standards..., 2012)*. The new rules were considered necessary to announce the role and powers of the remuneration consultant supporting the remuneration committee. There should also be disclosed information concerning the form of arrangement and recommended level of remuneration of executive directors. However, it is not necessary to disclose this information if the consultant of the organization only dealt with issues of discrimination. The information of the consultant, who drew attention to the link between the remuneration of executive directors with the issuer, which may lead to a conflict of interest, should be disclosed. It was necessary to disclose the relevant information concerning the remuneration committee:
 - information concerning the independence of the members of the committee,
 - financing the committee and the people supporting their activities,
 - analysis of the independence of the consultants that support the activities of the committee,
 - the way of remuneration and supervision of the consultant.

The recommendation of the independence committee on remuneration relates to all committees apart from limited partnerships, enterprises in bankruptcy and any foreign entities, in which there will be revealed the causes of the lack of an independent committee in the annual financial statement. The necessity of linking the members of the committee for remuneration with the company is connected with the notice (*Notice of..., 2013*) of the Securities and Exchange Commission in adapting the role of committees to the regulation Dodd – Frank Act. The document stated that each member of the remuneration committee should sit on the board of directors (as a non-executive director).

4. CONCLUSION

The financial crisis has highlighted the faulty structures of managerial staff remuneration systems in financial institutions. Unreasonable levels of remuneration could lead to a decline in the security of bank activity. The regulators in the European Union and the United States have introduced a number of regulations regarding the levels and structures of remunerations of executives in financial institutions. The effectiveness of these regulations may result in increased security of banks and linking remuneration with the results of the institution.

The European Commission should implement the recommendation on the need for the annual publication of a document on the remuneration policy of a given company. A separate document should contain all information received,

the annual remuneration and the implementation of other benefits from working for a company, each member of the management board and the supervisory board. Such a document should be published by a remuneration commission in the form of an annual activity report of the committee.

Abstract

The financial crisis has highlighted the faulty structures of managerial staff remuneration incentives and systems in financial institutions. Consequently, regulators in the European Union and the United States have introduced a number of regulations regarding the levels and structures of remunerations of executives in financial institutions. However, these recommendations were only an outline of the changes that should be made, not providing specific solutions in terms of implementation. Consequently, the paper analyses the effectiveness of these regulations and presents some recommendations.

Key words: Remuneration of bank managers, regulation of financial remunerations

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