Dock exec base pay for malfeasance: Carney

By JEFF BUCKSTEIN

Fed up with shareholders getting a raw deal as a result of bank malfeasance, Bank of England governor Mark Carney has called for executives of those institutions to be held more personally accountable.

Carney, speaking at the recent 2014 Monetary Authority of Singapore Lecture, cited the multibillion-dollar fines paid by major banks as a result of their misconduct in foreign exchange markets, which followed on the heels of another scandal involving massive penalties for institutions caught abusing interbank interest-rate benchmarks.

"The repeated nature of these fines demonstrates that financial penalties alone are not sufficient to address the issues raised. Fundamental change is needed to institutional culture, to compensation arrangements and to markets," said Carney, who is also chair of the Financial Stability Board, and a former governor of the Bank of Canada.

"The public were rightly angered that so many leaders and senior managers who were responsible for sowing the seeds of the crisis, and for allowing cultures to develop in which gross misconduct took place, have walked away from their actions or inactions."


CARNEY

Carney proposed that new standards may be needed to put the non-bonus or fixed pay of senior bank officials directly at risk. Senior manager accountability and new compensation structures will help to rebuild much-needed trust in financial institutions, he said.

"In a diverse financial system, trust must also be rebuilt in markets. Behaviours that aim to undercut market mechanisms, such as collusion, the misuse of confidential information, or the manipulation of market prices and benchmarks, must be stamped out," Carney said.

This is a slight departure from many other calls for reform which have traditionally concentrated on compensation packages outside of base pay, such as stock options, which can reach into the tens of millions of dollars annually.

"What Mark Carney is talking about here appears to align with the things that we have been saying for years," said Stephen Erlichman, executive director for the Canadian Coalition for Good Governance (CCGG) in Toronto.

"It's not a novel concept. It's something that we think does make sense in the appropriate context and the board applying it in a way that makes sense for that company," added Erlichman, who noted that recoupment policies are becoming commonplace in the U.S. and Europe. They have also been adopted by a number of Canadian companies such as Loblaw Companies Limited, as outlined in the CCGG's 2014 *Best Practices for Proxy Circular Disclosure* report.

The CCGG's *Executive Compensation Principles*, published in January 2013, states that it "may be appropriate for boards to require the return of compensation previously awarded to an executive in the event of a material earnings restatement or other company-specific change that significantly reduces shareholder value."


ERLICHMAN

Erlichman said whether executives are on the line for incentive compensation or base salary stems from the same idea, because if a corporation such as a bank is fined for its actions, its shareholders ultimately wind up on the losing end.

"The conceptual thought process behind this is that somebody in the organization needs to take responsibility for this, whether or not that executive actually had specific fault," he said.

Janne Chung, an associate professor of accounting at York University's Schulich School of Business in Toronto, said banks have largely shifted from an executive bonus compensation structure to increased fixed pay as a result of negative publicity regarding the former.

Chung supports the concept of executives being held financially accountable for the actions of their subordinates, noting that even when malfeasance may have been caused by the direct action of more junior staff members, there are instances where it is hard to imagine these people could have acted alone, without tacit senior management approval.

"They may not have exactly OK'd it. But they created, fostered the culture that allowed it to happen," said Chung.

Therefore, she believes it is fair that, whether or not a senior manager such as the CEO is directly involved in or knew about malfeasance-related actions, that person needs to be held accountable for the culture of the organization.

"I teach my students that senior management sets the tone on top. And I think if the senior people are serious about ethics and not just pay it lip service, then it should filter down to the lower-level employees. I believe that putting senior management pay at risk will help. At least they will come up strongly against that behaviour," said Chung.