US Banks Defer 60% of Executive Bonuses

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The largest US banks are deferring more than 60 per cent of senior bank executives' bonuses, according to a survey by the Federal Reserve.

The new trend in bank pay comes after a crisis many blame on excessive risk-taking by bankers and traders who were compensated for taking short-term risks without having to suffer the long-term consequences of their actions. Financial regulators around the world initiated a crackdown.

Some of the most senior US bankers are seeing more than 80 per cent of their incentive compensation paid out over a longer time frame, the Fed said after surveying pay packages at 25 of the biggest banks doing business in the US.

While deferral periods typically last between three and five years and involve a mixture of cash and stock grants, a three-year stock deferral is the most common scheme, the Fed said.

Regulators argue this ensures employees keep their company's overall performance in mind when taking risks but pay expert Lucian Bebchuk of Harvard Law School reckons that stock grants simply incentivise bankers and traders to take bigger risks. The more risk taken, the greater the potential the bank's share price – and the value of the banker's bonus – will rise, he says.

Still, the new trend is a departure from pre-crisis practices, said Peter Miterko, managing director at compensation consultancy Pearl Meyer & Partners.

"Nothing was deferred. It was straight-up cash," Mr Miterko said. "You got your bonus cheque at the end of the year and that was it."

The pay consultant, who said he worked on five of the Fed's pay reviews, reckons the new trend is likely to reduce excessive risk-taking. Senior bank executives tend to agree, he said.

Among the changes in compensation practices is the inclusion of risk managers in setting bankers' and traders' pay, the Fed said.

Risk-takers, among the most lavishly compensated during the boom, are seeing their pay being adjusted for risk. So the more potential damage a bet may bear down the road, the more likely the trader's pay will be adjusted to reflect the downside.

The new trend is not limited to senior executives. At many firms, these new reviews involve the pay schemes of tens of thousands of employees, the Fed said. That was not the case when bank examiners began their review in 2009.

These lower-level employees are not likely to be as pleased with the new practices as their bosses, Mr Miterko said.

The US trend is generally in line with what regulators agreed to at the Financial Stability Board. By comparison, European rules are tougher on the front end – they limit cash compensation – but US practices may be tougher over the long term, as they generally involve stock grants over years, which may incentivise bankers to pay more attention to performance.