Banking and Finance Law Daily Wrap Up, DIRECTORS, OFFICERS AND EMPLOYERS—New York Department will monitor bank's incentive compensation, (Oct. 11, 2016)

Banking and Finance Law Daily Wrap Up

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The New York State Department of Financial Services has issued guidance to its regulated banking institutions requiring incentive compensation arrangements to be devised so that employees are not provided incentives to engage in unacceptable practices or conduct. The Guidance was initiated in the wake of the recent action against Wells Fargo, where employees secretly opened new accounts and funded them with transfers from existing ones without the knowledge or consent of the account holder.

New York Governor Andrew M. Cuomo stated that the "inappropriate behavior we have seen at institutions like Wells Fargo are the same ones that led to the 2007 financial crisis and there must be zero tolerance for reckless policies that foster greed and put New Yorkers' financial futures at risk." New York State Department of Financial Services Superintendent Maria T. Vullo said the Department will "take swift enforcement action against financial institutions with misaligned incentive compensation schemes that foster improper behavior among their employees."

The guidance warns that the failure of internal control functions to identify risks and shortcomings at a bank could lead to "disastrous outcomes for consumers and for the bank" from a safety and soundness and reputational risk perspective.

Minimum principles. Under the guidance, no incentive compensation may be tied to employee performance indicators without effective risk management, oversight and control. The guidance also highlighted the need for caution around cross-selling and referral bonus arrangements.

The following principles are the minimum standards that any incentive compensation arrangement at a bank must meet:

1. Balance Between Risks and Rewards: Any incentive compensation arrangement must appropriately balance risk and financial results in a manner that does not encourage employees to expose their organizations to imprudent risks.
2. Effective Controls and Risk Management: A banking institution's risk management processes and internal controls must reinforce and support the development and maintenance of any incentive compensation arrangements.
3. Effective Corporate Governance: Incentive compensation arrangements must be supported by strong corporate governance, including active and effective oversight by the organization's board of directors.

State banking examiners will conduct supervisory review of incentive compensation arrangements during the Department's regular risk-focused examination process.

Companies: Wells Fargo

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