Big Banks
Bonus Bonanza

NATIONAL PEOPLE'S ACTION

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Executive Summary

Once again, Wall Street is on track to pay astronomical bonuses to its star traders, even as the rest of America is reeling from the devastation the banks have unleashed on the global economy. These billion-dollar bonuses come at our expense, have no rational justification, and only serve to destabilize the larger economy. It is time to rein in banker compensation to get the economy working for Main Street again and to prevent another global economic catastrophe in the near future.

Bonus Bonanza on Wall Street. Wall Street is at it again in 2010, after paying out all-time record bonuses last year. The top six banks alone are on track to pay out $143 billion in bonuses and compensation this year, more than enough money to fill the entire $130 billion budget gap for every state in the country for FY 2011. $143 billion could create 3.6 million jobs if pumped directly into the economy. With just half of the money, the banks could reset the principals and interest rates on all underwater mortgages in the country to market rates, pumping $73 billion into the national economy.

- Total bonuses and compensation at the top six banks are just shy of the record set in 2007, even when accounting for the recent bank mergers.
- Meanwhile, the size of the workforce at these six banks has shrunk significantly as a result of consolidation in the industry. As a result, average compensation per employee at the top six banks has actually jumped more than 10 percent from 2007.
- The bonuses have not trickled down to front-line bank workers, such as tellers and call center operators; thousands of whom have been laid off or seen their wages stagnate.
- 37 percent of every dollar the top six banks take in gets set aside for bonuses and compensation. Around the country, many state and local governments are having to close libraries, lay off workers, and cut vital neighborhood services because they are stuck in toxic deals with banks that are costing them millions. For every million they lose to Wall Street, a banker gets $380,000 added to his paycheck.

Money for Nothing. It is a common myth that bankers are paid so well to reward them for the value they bring to their companies, which in turn grows the national economy. In reality, Wall Street's bonuses have actually created a financial sector that preys on the real economy. Bankers' billion-dollar payouts come from our pockets and put the entire economic system at risk.

- Bankers are middlemen and gamblers who make their billions by charging us exorbitant fees and by making speculative bets. Rather than producing anything of value to the real economy, they actually suck money away from Main Street and funnel it into their casinos on Wall Street. They make billions, but the pie gets smaller for the rest of us.
- There is little rhyme or reason to the bonuses that banks pay their top employees. Our study of compensation practices at the top banks shows there is no relationship between banker bonuses and performance.
- Runaway bonuses are not even good for the banks themselves. Wall Street's bonus structure promotes recklessness and excessive risk-taking, which has a destabilizing effect on banks and the larger economy.

Taking Back the Economy. Wall Street's bonus culture has kept Main Street from prospering for decades by diverting our nation's wealth to a fundamentally unproductive sector of the economy. It also incentivized bankers to take the excessive risks that eventually brought down the entire global economy. Now, while the rest of us are left cleaning up the bankers' mess, Wall

Street is paying out billions to its star traders. Those billions could have funded a real economic recovery on Main Street. It is time to take back the American Dream from the greedy bankers who are holding it hostage, and to rein in runaway banker bonuses.

Introduction

While ordinary Americans are suffering from foreclosures, layoffs and steep cuts in public services, the big banks are sucking up the nation's wealth and using it to award record bonuses to the same bankers that crashed the economy. By rewarding unproductive and destructive behavior, the Wall Street bonus culture has created a perverse system in which our national economy has become a slave to the masters of the universe, resulting in a massive transfer of wealth from Main Street to Wall Street.

This is highway robbery. Wall Street's billion-dollar bonuses come at our expense, have no rational justification and only serve to destabilize the larger economy. Banker compensation is a fundamental issue that must be addressed to prevent future crises and bring about a long-term, sustainable economy recovery for America's working families.

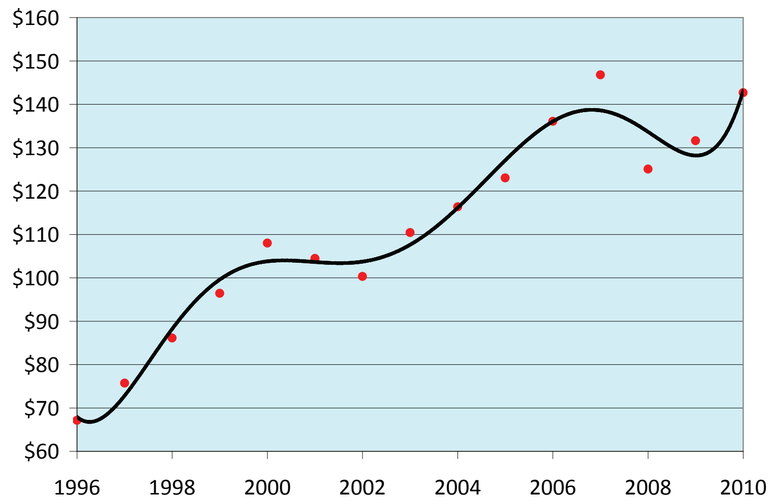
Bonus Bonanza on Wall Street

Despite unleashing havoc on the global economy, Wall Street is once again getting ready to pay astronomical bonuses this year. The nation's six largest banks alone are on track to pay their bankers a staggering $143 billion in bonuses, benefits and compensation ("bonus and compensation"),[1] more than enough to fill the $130 billion[2] total budget gap for all 50 states in FY 2011. **If Wall Street pumped this money directly into the economy instead of paying it to its bankers, it could create 3.6 million new jobs, and lower the unemployment rate by 2.3 percent.** Bank of America tops the list, with $35 billion in bonuses and compensation set aside for its bankers.

TABLE 1: Bonuses and Compensation at the Top Six Banks (2010)

Bank	2010 Bonuses and Compensation
Bank of America	$35.1 billion
Wells Fargo	$26.1 billion
JPMorgan Chase	$25.4 billion
Citigroup	$22.6 billion
Goldman Sachs	$17.5 billion
Morgan Stanley	$16.0 billion
Total for Top Six	**$142.7 billion**

GRAPH 1: Bonuses and Compensation at the Top Six Banks (1996–2010)



Even when controlling for recent acquisitions (Bank of America's purchase of Merrill Lynch and Countrywide; JPMorgan Chase's acquisition of Bear Stearns and Washington Mutual; and the Wells Fargo-Wachovia merger), 2010 compensation levels are near the high from 2007, when the six banks and the firms they have since acquired paid out $146.8 billion. Meanwhile, the size of the workforce at these banks has shrunk 12 percent, as the banks have eliminated 158,800 jobs, which means fewer people are making more money than ever before. [3] Average compensation per employee at these banks jumped more than 10 percent from 2007 to 2010. At JPMorgan Chase, the jump was even higher—nearly 16 percent.

However, while Wall Street is set to reward its top executives and traders handsomely in 2010, rank-and-file workers continue to get squeezed. Even though total compensation at the top six banks is up 14 percent this year from 2008, average real hourly wages for nonsupervisory workers in financial services have remained flat, rising less than 1 percent between December 2008 and October 2010.[4]

Even during the boom years before the collapse, executives took home a disproportionate amount of pay. The top five executives at each of the six banks saw their average compensation more than double from $9.8 million in 2001 to $22.5 million in 2007.[5] The bonuses did not trickle down to front line bank workers, such as the tellers who saw their real wages increase only 5 percent between 1999 and 2009.[6] In fact, like other hardworking Americans, thousands of front-line bank workers have been laid off or actually had their pay cut since the financial collapse in 2008.

Five million families have lost their homes to foreclosure thus far during the financial crisis. Nine million are expected to go into foreclosure between 2009 and 2012.[7] The foreclosure epidemic is no longer confined to just subprime borrowers or those at the fringes of the economy. As housing values continue to plummet and long-term unemployment becomes the norm, middle-class families with prime mortgages are becoming the new faces of foreclosure. With record unemployment and nearly a quarter of American homeowners under water with their mortgages, working families are losing their homes in record numbers.

Just Half of Wall Street Pay Could Solve the Housing Crisis

Experts agree the most effective way to stop the tsunami of foreclosures is through permanent, sustainable loan modifications that reduce homeowners' mortgage principal *and* interest rates to market value. Across the country, some 11 million homeowners are $766 billion under water with their mortgages. That means they owe $766 billion more on their mortgages than their homes are worth. If the banks were to write down their principals to market value and to refinance them into 30-year, fixed-rate loans at market interest rates, it would pump **$73 billion into the American economy every year for the next 30 years.** Over the life of the new loans, it would save Americans more than $2 trillion monthly mortgage payments. Homeowners could use this $73 billion to increase spending, invest in their small businesses and help turn the economy around. It would be a $73 billion annual stimulus, at no cost to taxpayers.

Moreover, the $73 billion it would take to reset *all* underwater homeowners' principals and interest rates would be about half of the $143 billion the top six banks alone are getting ready to pay in 2010 in bonuses and compensation. Even if the top six banks were to absorb the full cost of modifying all underwater mortgages in the country, they would still have $70 billion left for bonuses and compensation. Instead of taking home $12.6 million like he did last year,[8] JPMorgan Chase CEO Jamie Dimon would take home $6.1 million. He would still be one of the highest paid men in America.

> ***Even if the top six banks were to absorb the full cost of modifying all underwater mortgages in the country, they would still have $70 billion left over for bonuses and compensation.***

From Our Pockets to Theirs

Since 1999, nearly 37 percent of all revenues at the top six banks have gone straight to bonuses and compensation (see Table 2). What does that mean? It means that 37 cents out of every dollar that we have paid the banks—in ATM fees, in credit card interest, in late fees—has gone toward fueling runaway banker pay. This is also true of state and local governments that do business with banks. In California, state and local governmental entities are losing more than $540 million a year to banks on toxic deals known as interest rate swaps. $199 million of that goes straight from taxpayers' pockets to banker pay. In Michigan, interest rate swaps are costing taxpayers $132 million a year, and $49 million of it goes straight to bankers' fat paychecks. Banks don't charge us billions in fees just to cover their own costs of providing us with services; they charge us billions more than they need because they put 37 cents of every dollar we pay them into their bonus and compensation pools. So while cities across the country are closing down libraries and making difficult choices about whether to lay off police officers or firemen, our tax dollars are funding big paydays on Wall Street.

The GOP's Gift to Wall Street

Wall Street typically doles out bonuses in January. This year, however, banks such as Goldman Sachs seriously weighed paying its bankers in December so they would not have to pay higher taxes if the Bush tax cuts were allowed to expire at the end of 2010.[9] At the same time they are talking about making cuts to Social Security, Republicans in Congress are fighting hard to ensure the tax cuts are extended for the wealthiest 2 percent of Americans, an elite group that includes our big bank CEOs. U.S. Chamber Watch has estimated how much the CEOs of some of the biggest financial firms will save under the tax cuts.

Bank	CEO	Windfall from Bush Tax Cuts
Goldman Sachs	Lloyd Blankfein	$1.66 million
American Express	Kenneth Chenault	$1.33 million
JPMorgan Chase	Jamie Dimon	$1.18 million
State Street Bank	Jay Hooley	$1.07 million
Bank of New York Mellon	Robert Kelly	$955,000
Morgan Stanley	John Mack	$926,000
Charles Schwab	Walter Bettinger	$882,000
Wells Fargo	John Stump	$813,000
Citigroup	Vikram Pandit	$785,000

Banks Used Taxpayer-Backed Profits to Justify Bonuses

Even though most of the big banks returned TARP in 2009, their 2010 bonuses and profits were still based heavily on taxpayers' generosity. The $700 billion TARP was just one of many bailout programs, and nowhere near the largest or most significant.[11] The Federal Reserve released data in December 2010 detailing $3.3 trillion in emergency loans it made to banks during the economic crisis.[12] In all, the banks received $17 trillion in bailouts and backstops from American taxpayers. For example, big banks' trading profits are a direct result of the Federal Reserve's decision to use $1.25 trillion of public money to buy mortgage-backed securities.[13] Banks are now using those profits to justify large bonuses. Furthermore, without taxpayer support, the banking industry would have collapsed in 2008,[14] and there would have been no money left for bonuses in 2009 or 2010.

Happy Days Are Here Again

> **Wall Street bankers hiring a dwarf for an over-the-top bachelor party in Miami. Nieman Marcus selling out its 100 limited-edition $75,000 Camaros in three minutes. Socialites dropping $40,000 on a custom cell phone at a jewelry store in Chicago. An investment analyst at Goldman Sachs who hired hip-hop queen Lil' Kim to perform for 1,000 guests at his annual Halloween party last month.**
>
> **What is this—2006?**
>
> **Though the unemployment rate remains near 10 percent with millions of Americans about to run out of their jobless benefits, one in five Americans are using food stamps to buy groceries and small businesses are being forced to slash their work forces to stay alive, Wall Street's top bankers and wealthy investors are spending to excess, indulging their every whim.**
>
> -*Huffington Post*, Nov. 24, 2010[15]

Money for Nothing

In November 2009, Goldman Sachs CEO Lloyd Blankfein told a room full of bankers in London that the firm's lavish and excessive compensation structure was justified because "The people of Goldman Sachs are among the most productive in the world."[16] In 2010, even after their business practices helped throw the global economy into a freefall, Goldman employees will take home an estimated $513,118 in compensation on average. Meanwhile, median income for American workers was $28,365 as of 2009.[17] If you apply Blankfein's logic, Goldman employees took home more than 18 times as much as the median American worker because they are more "productive."

Bankers' bonuses at Goldman and other banks are often justified as necessary to retain the top talent. Bankers, we are told, make so much money because they have a special skill set that helps their companies make billions in profits, and in turn grows our national economy. This is simply not true. A closer look demonstrates that (1) the modern financial sector consists primarily of middlemen who make their money, not by producing anything valuable, but by taking money from the rest of us and using it to make risky bets; (2) there is no relationship between banker bonuses and performance and that Wall Street rewards failure just as handsomely as it does success; and (3) the big banks' bonus structure actually encourages reckless behavior that puts the entire global economy at risk.

The "Most Productive" People in the World

So what is it that Blankfein's "most productive" people in the world actually produce that justifies Goldman's outrageous bonuses? Automakers make our cars. Farmers grow our food. Construction workers build our homes. Janitors clean our offices. Doctors and nurses provide us with healthcare. They are all productive members of our society and the work they do has value in the real economy.

The largest parts of the financial sector, however, do not actually produce anything. At this point a very small portion of money is actually made in the traditional business of lending money to the drivers of the real economy. Instead, banks bring in large amounts of money by creating and selling exotic financial products, and through fees they attach to consumer banking and even public finance. Much of this money never gets reinvested into the real economy and just cycles through from one Wall Street firm to another. As the American economy has grown more dependent on finance, we have seen a big transfer of wealth from Main Street to Wall Street.

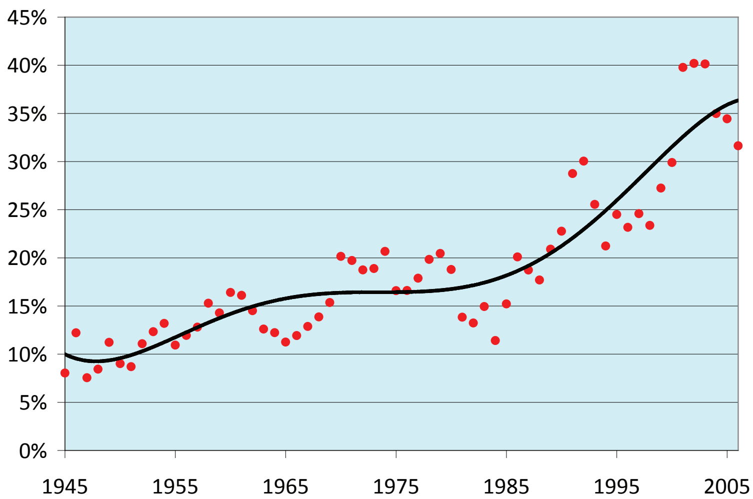
Historically, when the real economy did well, so too did Main Street. Until about 30 years ago, corporate profits were firmly rooted in the goods and services produced by workers. Because workers were compensated fairly for their labor, they could afford to buy these same goods and services as consumers, thus creating a demand that stimulated the economy. This cycle, in which workers produced the supply and then used their wages to create the demand allowed the real economy to grow. However, the dismantling of fundamental worker protections in the 1970s led to declining unionization rates across the country. As unions lost clout, worker wages stagnated. Rather than paying workers fair wages, CEOs increasingly started keeping more for themselves and investing the extra money into the financial sector.[18]

Les Leopold explains this phenomenon in his book, *The Looting of America: How Wall Street's Game of Fantasy Finance Destroyed Our Jobs, Pensions, and Prosperity and What We Can Do About It*:

> [P]roductivity increases and wages were decoupled during the 1970s. As a result, trillions of dollars in surplus capital went to the investor class because average real wages failed to rise along with productivity. There was so much surplus capital held in so few hands that it could no longer find solid investments in the production of goods and services. (Had it gone to working people, there would have been more spending on real goods and services, and more investment opportunities in the real economy.) Instead, it then funneled into the fantasy-finance casino. Clouds of financial instruments were created to suck up piles of surplus capital, and this put us all at risk.[19]

As wages have stagnated, the financial sector has grown substantially larger. In 1979, the finance, insurance and real estate (FIRE) sector accounted for 21 percent of all corporate profits in the United States. By 2006, the height of the housing bubble, it had come to account for 32 percent. Finance profits tumbled once the housing market started to turn in 2007, but by the third quarter of 2010, they were back up and finance accounted for nearly 29 percent of corporate profits.[20]

GRAPH 2: Financial Industry's Share of Total Domestic Profits (1945–2006)



This trend has fundamentally altered the business model for both commercial banks and investment banks alike.

Commercial Banks vs. Investment Banks

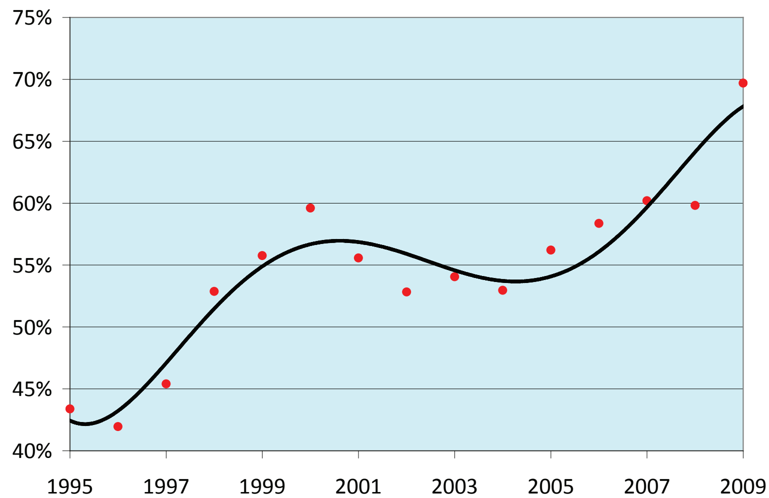
A commercial bank is what generally comes to mind when most people think of banks. It is a bank that takes deposits and makes commercial loans.[21] The four biggest commercial banks in the United States are Bank of America, JPMorgan Chase, Wells Fargo and Citigroup. Although all four of these banks also own investment banks, in the United States, they are regulated as commercial banks because that is their primary line of business in this country.

Investment banks are the firms that raise capital for deals, advise major corporate clients, underwrite bonds, manage corporate mergers and acquisitions, and trade complex securities and derivatives. This last function was their undoing in 2008. On January 1, 2008, there were five major standalone investment banks in the United States—Goldman Sachs, Morgan Stanley, Merrill Lynch, Lehman Brothers and Bear Stearns. In September 2008, there were only two—Goldman Sachs and Morgan Stanley. By Jan. 1, 2009, there are none left as Goldman Sachs and Morgan Stanley became bank holding companies so they could have access to cheap money from the Federal Reserve as well.

Commercial Banks Take Our Money …

The basic function of commercial banking is to take in money from depositors and loan it to borrowers. In the past, banks made the bulk of their money by charging borrowers a slightly higher interest rate than the paid depositors and then booking the difference as profit. However, this changed drastically over the years. While many community banks still function this way, today's big banks drive a much larger share of their revenues from noninterest income, such as fees.

GRAPH 3: Reliance on Noninterest Income at Top Three Commercial Banks* (1995–2009)

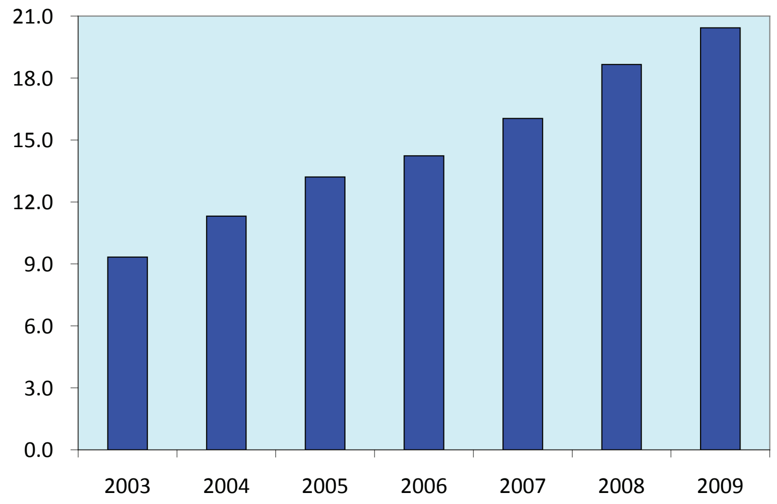


**Includes Bank of America, JPMorgan Chase, and Wells Fargo.*
Citigroup was excluded because it has a large global presence and while it is a major commercial bank domestically, commercial banking makes up a substantially smaller portion of its business globally.

While this new business model has meant increased revenue for banks, it has done nothing to grow the economy. In fact, it has drained money out of the real economy and deposited it directly into bankers' pockets.

In order to maximize fee income, banks have come up with new types of fees to nickel-and-dime Americans wherever possible. Customers are routinely hit with overdraft fees, ATM fees, fees for talking to a bank teller,[22] fees for using a PIN to charge a debit card,[23] fees for requesting copies of canceled checks,[24] fees for depositing a bad check that someone else wrote,[25] fees for requesting to speak with a live service representative rather than an automated machine,[26] and even fees for paying credit card bills over the phone.[27] While the Dodd-Frank Wall Street Reform and Consumer Protection Act and the establishment of the Consumer Financial Protection Bureau (CFPB) should help curb some of these abuses, for years, the banks are already trying to find new ways to make up the lost revenue. As a result of these new tricks and traps, fee income at the top four commercial banks more than doubled between 2003 and 2009, going from $9.3 billion to $20.4 billion.[28] The banks did not do anything truly productive to earn the money from these fees.

GRAPH 4: Fee Income at the Top Four Commercial Banks, in Billions of Dollars, (2003–2009)



While these fees boost banks' bottom line (and help executives line their own pockets with bonuses) they have a pernicious effect on the rest of the economy. Every year, Americans pay tens of billions of dollars in bank account fees. In 2009, Americans paid an estimated $38.5 billion in overdraft fees alone.[29] That is $38.5 billion they did not spend buying groceries, clothes, or new cars. Thus, bank fees decapitalize the real economy, moving money out of consumers' pockets and into bank coffers. Banks, in turn, use that money to pay large bonuses to their top employees, who accumulate more money than they can possibly spend productively.

The Productive Role of Banks: Small Business Lending

Even though today's big banks derive most of their profits from fundamentally unproductive enterprises, they do still have a productive role in the real economy. Theoretically, they are still the ones who take money from depositors and lend it to small businesses on Main Street that produce real goods and services. However, this is a role the big banks have been neglecting as of late. Over the past two years, Small Business Administration (SBA) lending at the largest commercial banks (Bank of America, JPMorgan Chase, Citigroup and Wells Fargo) has plummeted. The decline has been most stark since the banks received bailout funds, presumably so they could start lending again. In FY 2007, together these four banks made 25,597 loans through the SBA 7(a) program. In FY 2008, these banks made only 12,708 SBA 7(a) loans—less than half the number of loans provided the previous year. In FY 2009, the number of small business loans from these four banks dropped an additional 61 percent to 3,743, and this despite the fact they had absorbed other banks such as Washington Mutual and Wachovia that provided small business lending as well.

... And Investment Banks Gamble It Away

Traditionally, investment banks only traded on behalf of their clients; they did not trade with their own money. However, as the financial sector grew in size and the investment banks saw the outsized returns they were bringing in for their clients, they wanted a piece of the action. They began trading with their own money to generate revenue for the bank itself. This is known as proprietary trading.

In addition, the investment banks realized they could rake in outsized fees by "engineering" newer and more complex financial products for the ballooning investor class. These products appeared more and more profitable, even though no one really understood what precisely the products were or how they created value and eliminated risk. As long as the firms' revenues soared, and bankers' bonuses were up, Wall Street was happy.

In the last decade, investment banks made (and then lost) billions of dollars creating and trading these exotic financial products. From asset-backed securities (ABS) such as collateralized debt obligations (CDO), collateralized loan obligations (CLO), structured investment vehicles (SIV), securitized leveraged buyout (LBO) debt, and mortgage-backed securities (MBS) to derivatives such as credit default swaps (CDS), interest rate swaps, and oil futures, to the synthetic CDO that has been derided as the "unholy spawn" of a CDO and a CDS,[30] investment bankers were gambling on an alphabet soup of explosive products (TNT) that eventually blew up not only the financial economy on Wall Street, but also the real economy on Main Street.

In essence, the bankers made bets on events in the real economy—whether homeowners would default on their mortgages and whether companies such as General Motors would go under[31]—but they did not produce anything that added value to the real economy. Homeowners were no less likely to default and General Motors was no less likely to go bankrupt because of bankers' bets. Arguably, the opposite was true because of the destabilizing effect these bets had on the real economy.

Do Even the Bankers Know What They Are Doing?

Similarly, in 2008, oil futures drove the price of gas to over $4 per gallon. This wasn't because of supply shocks. In the six months before prices spiked, global oil supply was increasing and demand was decreasing. Gas prices jumped to astronomical heights because bankers went on a gambling binge. As *Rolling Stone* reported, "By 2008, a barrel of oil was traded 27 times, on average, before it was actually delivered and consumed."[32] These bets did not make gas more efficient or any cleaner. They just drove up the price for the rest of us.

While Lloyd Blankfein may believe his bankers are among the "most productive" people in the world, in reality bankers are producing little other than devastation on Main Street. The financialization of the economy, fueled by distorted compensation structures and excessive bonuses, has resulted in trillions of dollars of wealth being moved from the real economy to the finance economy, from Main Street to Wall Street.

Some of the "financial instruments" that bankers trade are so complicated, even they cannot figure how they work or explain why they make or lose money. For example, Wells Fargo has taken out derivatives to hedge against losses on a certain pool of mortgage-servicing rights. The two should function like opposite sides of a see-saw; if one goes up, the other should go down. The idea is that gains from one should offset losses from the other, so the bank can limit its exposure to risk. However, Wells Fargo's derivatives see-saw seems to defy the laws of physics. *Bloomberg News* columnist Jonathan Weil reported in January 2010:

> A strange thing happened last quarter at Wells Fargo & Co. A bunch of derivatives that were supposed to act as hedges on other assets seemed to go berserk.
>
> The good news for Wells shareholders is that the oddly behaving derivatives boosted the bank's fourth quarter earnings … The hedges and hedged items both went up. This

> scenario should have been as likely as both sides of a see-saw rising at the same time … For all we know, there could come a time when Wells' derivatives misbehave at the same time the market values of the mortgage-servicing rights plunge. That would mean a double hit to earnings, rather than a windfall. Oh, but what are the odds of that happening, since Wells seems to have it all figured out?[33]

If Wells Fargo can't explain why its derivatives' value goes up or down, then it is flying blind, with $1.2 trillion in assets34 and an implicit taxpayer guarantee to boot.

No Rhyme or Reason

Wall Street has long argued that billion-dollar bonuses are necessary to reward the best of the best and that Wall Street's performance justified the lavish payouts. However, the crash of the financial markets shows just how false that assertion has been. The same year that the big banks crashed the economy and went to Uncle Sam, hat in hand, asking for a bailout, the top six banks paid $125 billion in bonuses and compensation.

In his July 2009 report on Wall Street bonuses, N.Y. Attorney General Andrew Cuomo wrote of Wall Street's "heads I win, tails you lose" bonus system:

> [T]here is no clear rhyme or reason to the way banks compensate and reward their employees …[I]n these challenging economic times, compensation for bank employees has become unmoored from the banks' financial performance.
>
> Thus, when the banks did well, their employees were paid well. When the banks did poorly, their employees were paid well. And when the banks did very poorly, they were bailed out by taxpayers and their employees were still paid well …

We analyzed bonuses and compensation at the top six banks and the firms they have acquired to see how compensation structures helped bring Wall Street to its knees. We started our analysis with the repeal of the Glass-Steagall Act in 1999, which allowed today's financial supermarkets such as Bank of America and Citigroup to be created.

Our analysis backed up Cuomo's assertion that there is no relationship between banker compensation and bank profits. Instead, compensation seems to correlate with overall bank revenues. For the top six banks, total bonuses and compensation hovered around 35 percent of revenues until 2006, after which they started going all over the map because of disruptions in the markets caused by the economic crash. In contrast, compensation as a percentage of profits fluctuated between 130 percent and 303 percent. This means that in the run up to the crash, bankers' pay was roughly 35 percent of how much they took in, even if their deals went bad down the line and ended up losing money. That's like getting paid for placing a bet, whether or not your bet wins.

TABLE 2: Compensation vs. Performance at the Top Six Banks (1999–2010)

Year		
1999	32.9%	157.6%
2000	35.5%	181.9%
2001	35.8%	209.8%
2002	33.4%	162.7%
2003	33.0%	132.8%
2004	31.4%	135.0%
2005	33.3%	130.7%
2006	34.7%	131.3%
2007	42.1%	263.0%
2008	70.5%	N/A*
2009	36.9%	303.3%
2010 projected	38.0%	270.1%
Total	**36.8%**	**213.3%**

**The banks did not make a profit in 2008, so the $125 billion in bonuses and compensation they paid did not bear any relationship to profits whatsoever. Due to the financial crash, the banks overall reported a net loss of$75 billion for the year.*

Putting Bankers Ahead of Shareholders

The problem is even worse for banks' top executives. The banks' executive compensation structure appears to show little or no relationship with either revenues or profits. Bonuses and compensation for the top five executives at each of the top banks nearly doubled between 1999 and 2007, from $343 million to $674 million. Even though bank profits started to plummet starting in 2007, the top executives' compensation did not come back down until 2008, when Congress placed restrictions on executive pay as part of the TARP bailout. Some studies actually suggest that higher CEO pay may actually hurt companies. Researchers at Purdue University and the University of Utah found the more CEOs were paid, the worse their companies performed. This was especially true where a greater proportion of a CEO's compensation was in the form of incentive pay, or bonuses.[37]

Interestingly, in 2009, Citigroup's excessive bonuses and compensation actually wiped out profits for the whole year. The bank paid out $25.0 billion in bonuses and total compensation, despite posting a $1.6 billion loss last year. If the bank had cut its compensation by even 25 percent, it could have posted a $4.6 billion profit. By choosing to pay out lavish bonuses, Citigroup put its bankers ahead of shareholders.

Similarly, while Bank of America paid out $28.7 billion in bonuses and compensation in 2009, and on track to pay out $35.1 billion in 2010, its common stockholders only got a 1 cent dividend for each of the last four quarters, even though the bank has been free to pay more.[38] Under TARP rules, Bank of America was restricted to paying a 1 cent dividend to its common stockholders. After returning its TARP funds in December 2009, Bank of America has been free to pay shareholders higher dividends, but has consistently chosen to spend the money on bonuses instead.

Rewarding Risk

Wall Street's bonus culture is not even good for the banks themselves, and actually encourages bankers' destructive behavior. Wall Street's wizards made billions in bonuses over the years precisely *because* they took risks that crashed the economy. Economist Robert Frank explains:

> A money manager's pay depends primarily on the amount of money managed, which in turn depends on the fund's rate of return relative to other funds. This provides strong incentives to invest in highly leveraged risky assets, which yield higher average returns. But as recent events have shown, these complex assets also expose the rest of us to considerable systemic risk.
>
> On the balance then, the high pay that lures talent to the financial industry may actually cause harm.[39]

Indeed, Wall Street's bonus structure incentivized short-term profits over long-term stability. We've already seen that investment bankers' bonuses bore no relationship with long-term performance. They got their bonuses based on how their trades performed in the short run, and if their bets went bad a couple of years down the road, they got to keep the money anyway. This encouraged excessive risk-taking, since the bankers' trades only had to perform well until they were paid their bonuses. This perverse compensation structure has been identified as a culprit in the economic crisis.[40]

This was also true for the large commercial banks. Because of securitization, commercial banks were able to offload the risk from their loans they made to investors. As a result, lending standards plummeted because the banks got to collect hefty origination fees up front, and they did not have to worry about whether the borrowers could actually afford to pay back the loans down the line.

In order to increase their compensation, commercial and investment bankers alike fueled this high risk system. Each of the top six banks helped create the housing bubble, either by making subprime loans itself or by financing the major subprime lenders and then securitizing the loans. A similar story also unfolded in corporate finance. Banks started making "covenant-lite" loans to private equity firms, which were essentially corporate low-documentation loans. To hide the risk and avoid regulatory requirements, the banks moved these risky loans off their books by placing them in "structured investment vehicles."[41] Motivated in part by the ever-growing bonuses, the entire financial sector took on more risk than ever before. When the bankers' bets soured, taxpayers were stuck with the bill.

> **"In the three years before the crisis, the five Wall Street giants set aside a total of $295 billion in compensation. Had they not handed out bonuses or shifted more compensation into stock, pay experts estimate, those banks might have kept $118 billion of additional capital in the financial system. That is almost equal to the $135 billion of bailout funds that taxpayers poured into those five institutions."**
>
> -*New York Times*, Jan. 27, 2010[42]

Stock-Based Compensation Has Not Really Helped

It is widely believed that increasing the proportion of CEO pay in stocks and stock options can decrease risky behavior by aligning CEOs' own personal incentives with shareholder interests. While stock-based compensation is preferable to cash, it has not effectively prevented CEOs from risking their companies' health (and that of the larger economy) for personal gain. CEOs and other executives have been able to structure their stock and stock option rewards to act almost like cash in some instances. They have also been able to structure their pay packages so they gain all of the upside if they drive the stock price higher in the short term, but the bank would have to suffer tremendous losses for him to lose money, making the possibility of a downside appear too remote to be taken seriously. While some firms have changed their pay packages to focus on more long-term performance, serious flaws remain.

As a result of this misalignment of interests between executives and investors, CEOs have been able to reap millions in profits, even as their companies tumbled. In fact, even when Lehman Brothers and Bear Stearns collapsed, their CEOs came out ahead because they had already cashed out much of their stock before the companies bottomed. Between 2000 and 2008, the CEOs of Bear Stearns and Lehman—just two men—collected $920 million from stock sales and cash bonuses, even as they drove their banks into the ground.[43]

Taking Back the Economy

Wall Street's bonus culture had already caused untold damage on Main Street long before the economic crisis hit. The allure of bonuses ushered in a new era in which big banks turned a profit by taking our money and gambling it away. On an individual level, this has taken real money from our pockets—money we could have used to send our kids to college, buy health insurance, or save for retirement.

On a national level, it has impeded us from putting our money to more productive uses such as investing in green technologies or finding a cure for cancer. Bank bonuses have also caused a brain drain in the real economy as thousands of college graduates increasingly leave behind careers in engineering or medicine and follow the money to Wall Street instead.[44] Even before the crash, Wall Street's bonus culture had sucked up so many resources there weren't enough left for anything else.

But over the last couple of years, we have seen the bonus culture has also created massive amounts of risk that was capable of bringing down the entire global economy. For us, it did. Unemployment and personal bankruptcies have reached levels not seen in years.[45] Foreclosures and food stamp usage are at record highs.[46] Small businesses are struggling to make ends meet because banks have cut back on lending,[47] and 48 states have struggled through budget crises the last two years.[48] Many have had to cut essential public services as a result.

And now, while bankers use taxpayer assistance to enrich themselves instead of jumpstarting the economy by lending, federal, state and local governments struggle to find the resources to clean up the banks' mess, protect services and create jobs. If even a fraction of the big banks' $143 billion in bonuses and compensation were used to fund important policy priorities, we could bring about a real economic recovery in this country:

- If $143 billion were injected directly into the economy as a cash stimulus, it could create 3.6 million jobs, at no cost to taxpayers.

- Just half of the money the top six banks are getting ready to pay in 2010 would provide the $73 billion needed to give all underwater homeowners in the country loan modifications with principal and interest rate reductions to market value.
- The banks' bonus and compensation pool for 2010 is more than enough to fill the $130 billion budget gap in every single state for FY 2011.
- Just 28 percent of the total payout could finance a $40 billion federal jobs initiative to create 1 million jobs in early childhood education, in-home services for the elderly and people with disabilities, and other community services.
- $10 billion, less than a third of what Bank of America alone is doling out to its bankers, could fund an increase to Head Start that would create 330,000 new jobs and better prepare children for school.
- The full $143 billion could extend unemployment coverage for each of the 15 million unemployed workers in the United States by more than seven months or buy individual health insurance plans for 65 percent of the nation's uninsured, changing the lives of more than 29 million people in the process.

$140.5 billion comes to $549 million each work day for bonuses and compensation. Even if the bankers donated just one day's pay to our communities, it could change lives.

- One day's pay at the top six banks could save 141,000 homes from foreclosure by providing mortgage payment assistance to struggling families.
- It could fund a 14-week extension of unemployment benefits for 134,000 laid-off workers.
- It would be enough money to fund full yearlong scholarships for 72,000 college students, allowing them to attend an in-state public university for free.

Taxpayers bailed out the big banks in their time of need and to thank us, they turned around and wrote billion-dollar bonus checks to the very bankers that had crashed the economy in the first place. Meanwhile, we are reaping the consequences of their bad behavior.

Bankers' runaway bonuses must be reined in so our nation's wealth can be put to more productive uses and we can all enjoy a sustainable economic recovery and long-term prosperity. Furthermore, curbing bankers' compensation is critical to safeguarding against future crises and protecting Main Street from Wall Street's self-destructive tendencies. It is time to rein in bank bonuses and start investing in the American Dream again.

Appendix

Potential Job Creation by Bank
See below to see how many good-paying jobs with benefits big banks could create if they spent their bonus on job creation instead of banker bonuses.[1]

Bank of America:	878,300
JP Morgan Chase:	634,200
Wells Fargo:	564,800
Citibank:	437,400
Goldman Sachs:	652,500
Morgan Stanley:	399,600
TOTAL:	**3,566,800**

1 Figures based on a cost of $40,000 per job.

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