

Reward and remuneration: Where was HR during the bonus fiasco?

The bankers' risk-taking and greedy bonus culture has been soundly condemned by the media. But how far was HR to blame? **David Woods** investigates what part they played.



Dona Roche-Tarry
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Protests, injuries, clashes with police, and one death. These were the chaotic scenes - reminiscent of the infamous poll tax clashes of the 1990s - of a besieged London on 1 April 2009. This time it wasn't government policy that sparked the ire of 4,000 protesters. Their fury was directed at a small legion of staff - the greedy City bankers who were pocketing huge bonuses as the country plunged into recession.

It's a far cry from the heady days of the late 1980s - glorified by the 1987 film, *Wall Street*. Michael Douglas won an Oscar for portraying the darker side of this industry as Gordon Gekko, a scheming megalomaniac taking part in risky deals and living by his now infamous affirmation: "Greed, for lack of a better word, is good". Skip forward 20 years to the City of London and it was Goodwin (Sir Fred) - and his £703,000 pension - not Gekko that came to personalise a sector, sick to the core, and bringing the country down with it.

But while much has been written about the leadership of these banks, surprisingly little has been said about HR's culpability as the people in charge of remuneration-setting. As investment banks and financial institutions are shamed in the press and their CEOs dragged across the coals, HR professionals have remained conspicuously silent. And it begs a question: where was HR when employees in the financial sector were being incentivised by their 'mega bonuses'?

When HR magazine approached the HR directors in some of the investment banks at the heart of the bonus fiasco, it was greeted by further silence. Goldman Sachs accepted a \$10 billion bailout from the US treasury last year. In July the bank announced it would be giving staff a pay and bonus pot of £12.3 billion. HR asked the bank how far its HR department was involved in the decision but a spokeswoman said it could not give any comment

on the subject of bonuses. It was a similar story at Morgan Stanley: "On this occasion we will decline to comment," it said.

What about Royal Bank of Scotland? In February it was reported to be paying out £1 billion to staff in bonuses. Less than a fortnight later, common sense seemed to have returned: awards to staff would now be based on sustained long-term performance, not short-term revenue generation. The bank's existing profit share bonus scheme has now been terminated so those associated with the 'major losses' of 2008 would not enjoy a pay increase or bonus. When HR asked the firm's head of HR, Neil Roden, to talk about his involvement in these issues, he was unfortunately 'unavailable'. Later, an industry insider suggested he "would not have been directly involved in remuneration issues" anyway.

Is that 'not directly involved', or involved but doesn't want to talk about it? Two-thirds of respondents in an HR magazine poll admit HR in their organisations does have a say on remuneration strategy, so are HRDs involved in bonus structures getting away with it?

Chris Roebuck, ex-global head of talent at UBS, and founder of Transformation, defends the banking elite. "There was no culture of greed in the banks," he asserts controversially. "The crisis happened because those at the top of organisations were not asking the right questions about what was going on. They didn't know the value of the deals they were working with."

Chris Bones, dean of Henley Business School, does not accept this. He says: "HR is complicit in designing remuneration strategy. The past 10 years has seen a long-term acceleration of greed regarding bonuses and HR sat on these boards and watched it happen."

So who's right? Although it is true HR directors are responsible for negotiating pay deals in most sectors, it is more unusual for HR to control remuneration in the financial services sector. This, says Jon Terry, partner and head of reward at PricewaterhouseCoopers, means the finger of blame cannot be pointed directly at HR departments in the financial sector: "In

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these organisations HR directors may not have been sitting on boards, but were represented by other board members. HR directors would probably not have been on remuneration committees. Although they are part of executive teams that run the business, the reward strategy would have been decided above their heads."

But Dona Roche-Tarry, managing partner at global search firm CTPartners and former head of HR for commercial banking at Barclays, says when she was an HR director she reported directly to the CEO. "The HR team should be held equally responsible for the issues with bonus strategies. They work alongside the CEO and MDs to recommend strategies for pay and bonuses particularly at executive level."

What is certain is that reward in the financial sector was out of kilter with the rest of the economy. In essence, traders and bankers received bonuses based on the volume of deals made rather than the profit they were bringing into the business. Alistair Milne, reader in banking at Cass Business School and author of *The Fall of the House of Credit*, explains: "Credit products are complex. HR was calculating bonuses based on something they did not fully understand. "

According to Terry, 80% of business leaders do not rate HR as an important strategic function and, if a department is not credible, its input on issues such as bonuses is not seen as being valuable. But if HR directors did not understand the credit products upon which bonuses were based, shouldn't they have made it their business to do so?

Roebuck explains: "To people on the street these structures look obscene, but it is not seen that way in the banking world. Banks lose staff because a competitor is offering an absolute fortune in a remuneration package."

According to Charles Cotton, adviser on reward and employment conditions at the CIPD, these market-led remuneration rates came at the expense of carefully thought-out and designed remuneration strategy.

Bones adds: "I think it is time for HR to eat humble pie. If a small number of people walk away with big money, HR is not doing its job properly. It should not have let itself be held to ransom by senior executives. If HRDs say they were not involved in remuneration decisions, then I say fire the HR departments."

Penny de Valk, chief executive of the Institute of Leadership and Management, agrees. "Why was HR not an active participant in discussions about remuneration?" she asks. "It is time for a more robust debate on the issue."

De Valk may be raising these questions, but at an industry-level at least the CIPD has been ambivalent about the issue. Initially, Cotton said: "HR wasn't involved in bonuses in investment banks a great deal." Then as HR was going to press, he announced that HR professionals should ensure executive pay packages do not lead to inappropriate risk-taking.

In August the prime minister, Gordon Brown, said bonuses for bankers should be based on long-term success rather than "speculative gains" and banks should claw back bonuses from staff reward over a period of time if their performance suffers.

But while governments in France, Germany and the US have taken steps to legislate against excessive bonuses, the Financial Services Authority (FSA) has said it will not get involved in the remuneration of individuals (see p28).

This puts the onus back on employers and there are lessons to be learned for HR directors across all parts of the economy to consider reward and recognition of staff more carefully to avoid a repeat of the events of the past two years. But if HR is to take part in educated debate it has to first prove its worth by suggesting strategic viable alternatives to 'mega bonuses' that still support the overall direction of the business. And some say they have lost this power to a growing raft of remuneration consultancies.

These consultancies have made a business out of advising employers on pay and reward. But Katharine Turner, principal at one such consultancy, Towers Perrin, defends her involvement: "I have seen articles suggesting 'too much power is imputed to consultants' but we are not business consultants - that is not what we do. And if boards did not understand the deals going on in their trading floors, how could we?"

It appears HR is also using lack of knowledge of the business as an excuse for its failings with bonuses. Turner explains: "FTSE 100 HR directors are not compensation experts. Their roots lie in people management not business management." However, she does add: "They have to get clued up."

The Walker Review released in July recommends more transparency in pay and bonuses in the City and codes released later by the FSA advocate less risky structures, with bonuses based on the longer-term. "I can't argue against transparency, but the codes are not as tough as I thought they would be," says Cotton. "The Government shouldn't get involved in bonuses because it could lead to unintended consequences."

The Treasury was unable to put a minister forward to comment but a spokesman said: "The chancellor has been clear that the

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short-term bonus culture must end. Reckless pay and bonus policies at banks right around the world contributed to the financial crisis. He will be taking forward Sir David Walker's proposals to reform the rules governing executive pay."

For HR to get the credibility it needs, David Coates, associate director at The Work Foundation, says: "HR has to become more than simply a compliance function. After the recession a new culture will come into the financial sector. HR does not necessarily have the authority to drive this culture, but HR directors can create a position for themselves as the custodians of fairness and concentrate on staff engagement."

HR directors in the financial sector must first consider what behaviours they are engaging. A more ethical performance from traders would be ideal and de Valk advocates reward for this behaviour "so people are not paid too much for doing the wrong thing", or more reward for teams rather than individuals. Milne and Roebuck suggest a percentage of bonus pots could be donated to charities rather than given to individuals. But retention is key as employers compete for talent, so some form of incentive will always be essential. Roebuck says: "Data suggests money is not always the main motivator anyway. Technical ability, respect of peers and subordinates as well as the regard of the boss can all incentivise."

HR has the potential to lead these initiatives. It may be only one voice on a board of directors - but a strong voice can make itself heard and receive the support it needs from other departments within business. Jane Shaw, MD of Resource Innovations, explains: "Remuneration is changing and we are seeing employers taking on HR staff who have the ability to understand the technical side of reward and the data management that comes with it.

"The role of reward professionals is evolving," she adds "These people will not be HR generalists. I think over the next five to 10 years, these reward directors will become HR directors, if they have the technical skills as well as

people management skills such as talent and retention management. A change in business structure will allow this."

This kind of business ability proves wrong the critics of HR who think it is mediocre and non-strategic. And Mark Adams, HR director of Abbey, is one of this breed of HR director who has moved from a background of reward. He explains: "I am still heavily involved in remuneration. I am the lead person on our HR team on that side and I am closely involved in how the FSA codes will be implemented at Abbey."

Abbey, now part of the Santander Group, has weathered the recession well, reporting a 25% increase in profits in April (See interview, HR, July 2009). Adams explains the company is made up 85% retail banking and 15% investment banking. He is quick to point out that retail banking and wholesale banking, despite the view of the FSA, are two different kettles of fish with regard to remuneration. But, he says: "It is important to remain competitive on pay in the financial sector although we have a risk structure that will never allow us to get into trouble."

At Abbey the employee value proposition is as much an important retention tool as bonuses. "In the past Abbey has been thought of as conservative (on pay) but we have proved ourselves to be virtuous and as a result can attract talent. People come to us because we are a prudent and safe place to work. We want longevity with our staff and I know we cannot achieve that through bonuses alone," adds Adams.

A sequel to Wall Street is planned to hit cinemas next year, according to the New York Times, and Michael Douglas will reprise his role. This time the setting is just before the crash of 2008 and Gekko will attempt to behave ethically.

Hindsight is a wonderful thing, but following deregulation of the financial sector in the 1980s and 1990s and the glory days of banking in London, few traders, or their HR directors, imagined the boom would end. It did, and now, as HR picks up the pieces of mass redundancies, manages talent and prepares for recovery, the opportunity has never been greater for this undervalued function to prove its worth and play its part in making sure a financial crisis of this scale will remain firmly in the past.