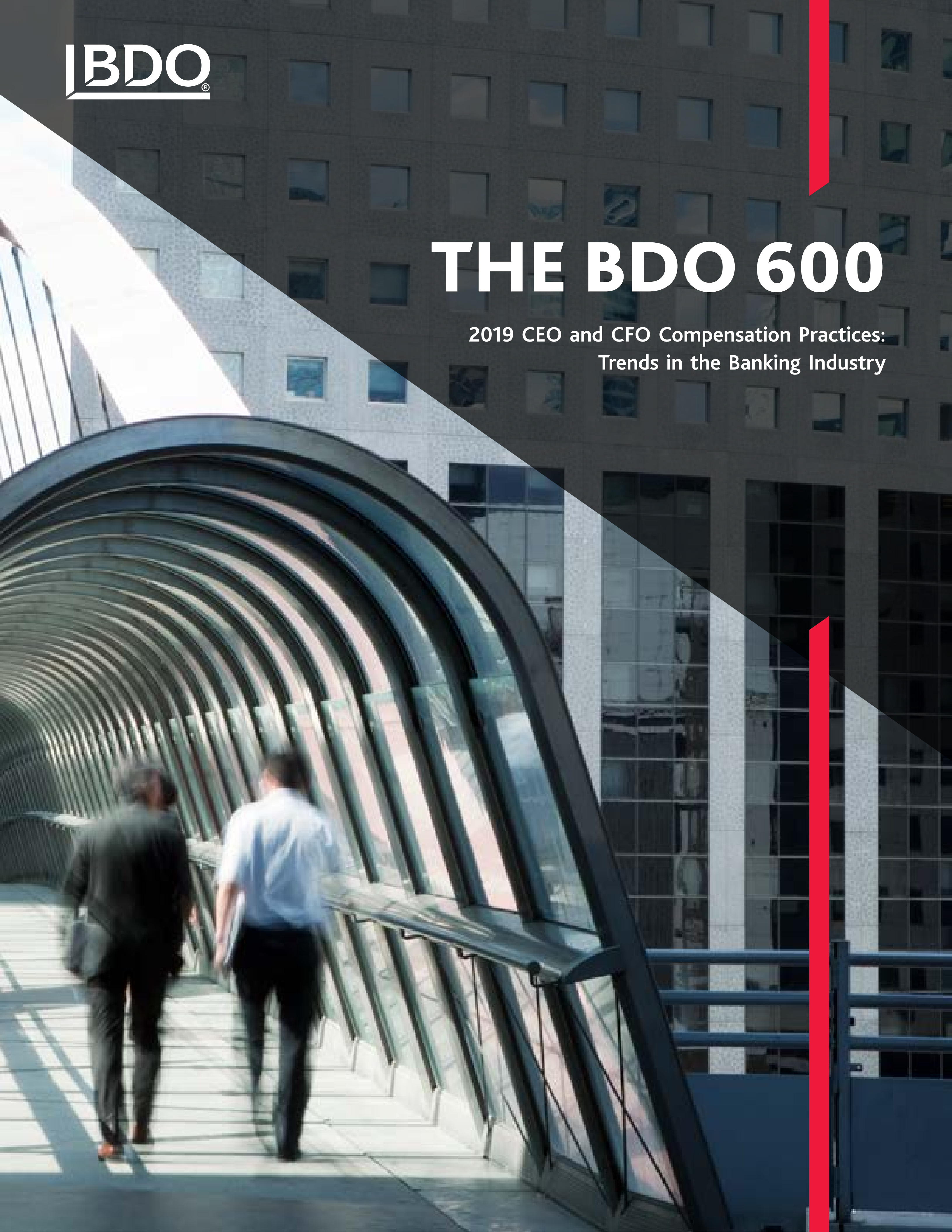
BDO

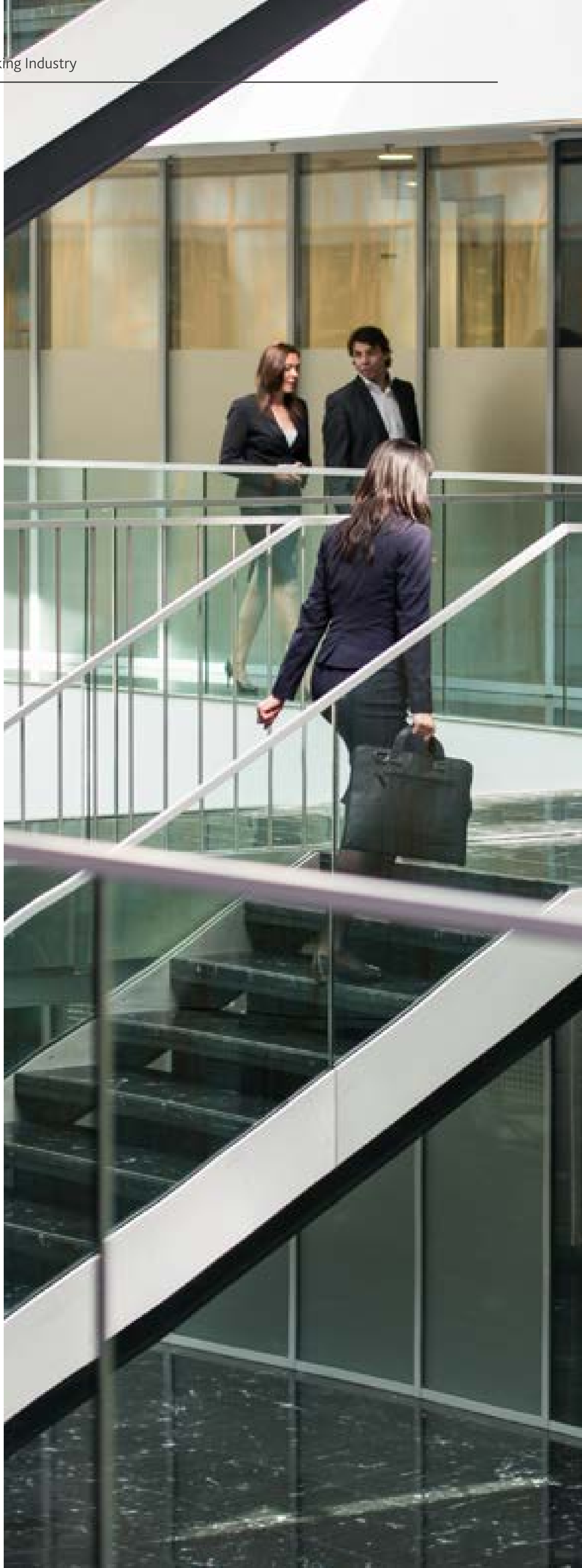
THE BDO 600

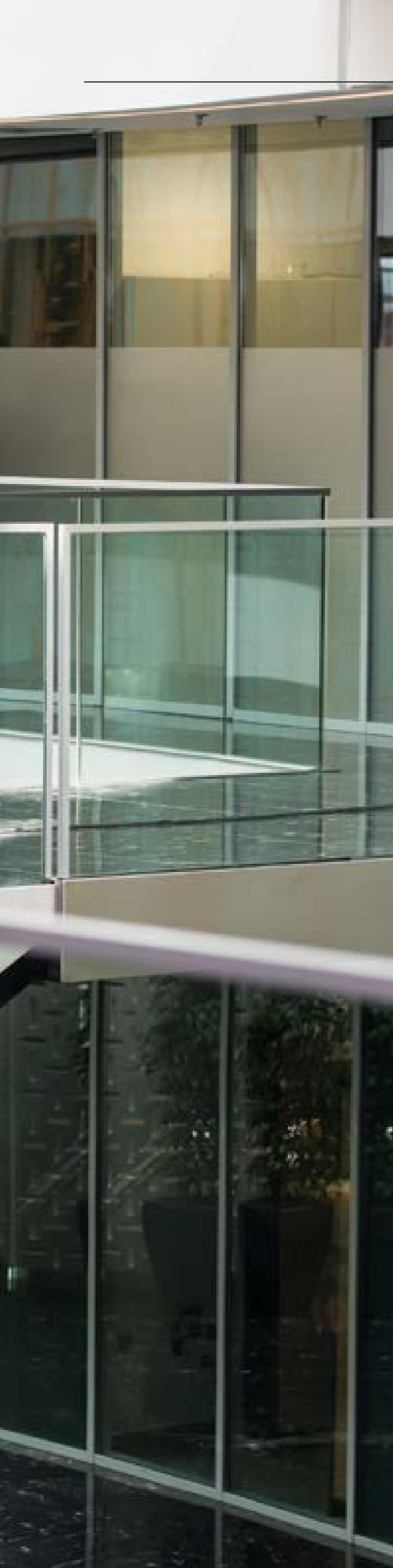
2019 CEO and CFO Compensation Practices: Trends in the Banking Industry



The banking industry continues to face many challenges related to legislative and regulatory changes, digital transformation, cybersecurity risks, new competitors and ultimately the need to reimagine its workforce. The new Current Expected Credit Losses (CECL) accounting standard and increases in the Fair Labor Standards Act (FLSA) salary threshold level and minimum wage have the potential to negatively impact overall earnings and profitability. However, macroeconomic growth, rising interest rates, increasing bank revenues and corporate profits, an increase in aggregate household debt, and consumer confidence all have positively influenced this very traditional industry.

These challenges and opportunities are reflected in the trends impacting banking industry CEO and CFO compensation, which remains the lowest relative to other industry sectors reviewed in this year's **BDO 600 Study of CEO and CFO Compensation Practices**. The traditional nature of the industry is reflected in conservative tendencies regarding the mix of pay, including greater emphasis placed on the cash component (base pay and annual incentives) over long-term incentives such as equity awards. Similar to past years, the mix of pay between total cash compensation and long-term incentive awards is approximately 75% and 25% for CEOs and CFOs, while the range for other industries is closer to 40% / 60% for the CEO and 45% / 55% for the CFO. For executives that receive long-term incentives, restricted stock continues to be favored over stock options, a trend that spans virtually every industry studied, and may be due to perceived volatility in the stock market making stock options less desirable.





This year's study found a notable increase in CEO and CFO compensation across all components of the total compensation package, with CFO compensation rising at a faster rate than CEO compensation. Total direct compensation (TDC) for CEOs saw an increase of approximately 7.6% over 2018, while TDC for CFOs rose approximately 16.3%. Although it is not clear why this occurred, it could be partially due to revenue growth and an uptick in profitability for community and regional banks. The substantial rise in CFO compensation resulted in a smaller pay gap in the ratio of CFO to CEO TDC over previous years (52% in 2019 versus 48% in 2018). Among the industries we reviewed, CFOs in the banking industry are the highest compensated in comparison to their CEO counterpart. This may be partially due to the relatively low level of CEO compensation as compared to other industries, which naturally brings CFO pay closer to this level. Another contributing factor may be that CFOs in the banking industry are often the second highest paid in terms of rank order relative to their position in the C-suite, whereas the COO is often rank-ordered second in other industries. This is due in part to the role that CFOs play in ensuring the appropriate amount of financial discipline and in managing risks related to internal controls. Another factor may be the responsibility of managing CECL implementation, which represents one of the most significant changes to banking regulations in recent history.

FINANCIAL SERVICES – BANKING INDUSTRY: CEOS

The average TDC paid to CEOs of companies in the financial services - banking industry for fiscal years 2018 and 2017 is listed below. Financial services – banking institutions provide the highest percentage of compensation in terms of salary and bonus/annual incentives among all industries studied. Average CEO (and CFO) compensation levels, however, remain the lowest of all industries included in our study. In 2018, CEO pay levels climbed upward.

Position	Year	Average Salary	Bonus + Annual Incentives	Stock + LTI*	TDC
CEO	FY 2018	$475,322	$209,564	$216,954	$901,841
	FY 2017	$446,505	$196,651	$195,104	$838,260
Change Over Prior Year		6.5%	6.6%	11.2%	7.6%

*Because not all CEOs received annual LTI payments, year-over-year comparisons may not accurately indicate market trends.

The resulting compensation mix is shown below.

Position	Year	Annual Cash	Stock + LTI	Total
CEO	2018	76%	24%	100%
	2017	77%	23%	100%

FINANCIAL SERVICES – BANKING INDUSTRY: CFOS

The average TDC paid to CFOs of companies in the financial services - banking industry for fiscal years 2018 and 2017 is listed below.

Position	Year	Average Salary	Bonus + Annual Incentives	Stock + LTI*	TDC
CFO	FY 2018	$270,025	$86,263	$111,220	$467,509
	FY 2017	$245,259	$77,136	$79,756	$402,151
Change Over Prior Year		10.1%	11.8%	39.5%	16.3%

*Because not all CFOs received annual LTI payments, year-over-year comparisons may not accurately indicate market trends.

The resulting compensation mix is shown below.

Position	Year	Annual Cash	Stock + LTI	Total
CFO	2018	76%	24%	100%
	2017	80%	20%	100%

Key Takeaways and Trends to Watch

The most notable trend in the banking industry is related to the Financial Accounting Standards Board's (FASB) **CECL accounting standard**, which is expected to improve financial reporting by requiring timelier recording of expected credit losses on loans and other financial instruments. However, it poses significant challenges as well, especially related to a bank's ability to accurately forecast expected losses in a volatile macroeconomic environment. The need to forecast expected credit losses will likely result in larger loan allowances and higher capital costs, which will almost certainly result in an upward trend when it comes to the pricing of products. This will have an impact on financial statements, which could ultimately impact performance-based incentive compensation plans, making goals more difficult to achieve.

Other notable trends include the ongoing need for digital transformation and the proliferation of online banking platforms and mobile applications, which have resulted in the closing of brick and mortar branches as consumers find alternative methods for meeting their customer service needs. Furthermore, there continues to be an increase in both traditional and non-traditional competitors such as savings and loans, thrifts, credit unions and other nonregulated diversified corporations and entities that offer financial services online and through other channels.

This has resulted in the need for community and regional banks to become more creative in the types and pricing of products offered. Finally, industry consolidation within the commercial banking sector has continued resulting in better-capitalized companies capable of offering a wider array of financial products and services at more competitive prices.

As a result of these trends we expect CEOs and CFOs who innovate and have the ability to think strategically about the type of transformation in which to invest a bank's resources will be the most highly-rewarded in the future. In such a competitive environment, attracting and retaining executives that can meet these demands will be dependent on good compensation strategies.

Planning for the Future

Moving forward, the key factors banks and their boards should consider with regard to compensation are as follows:

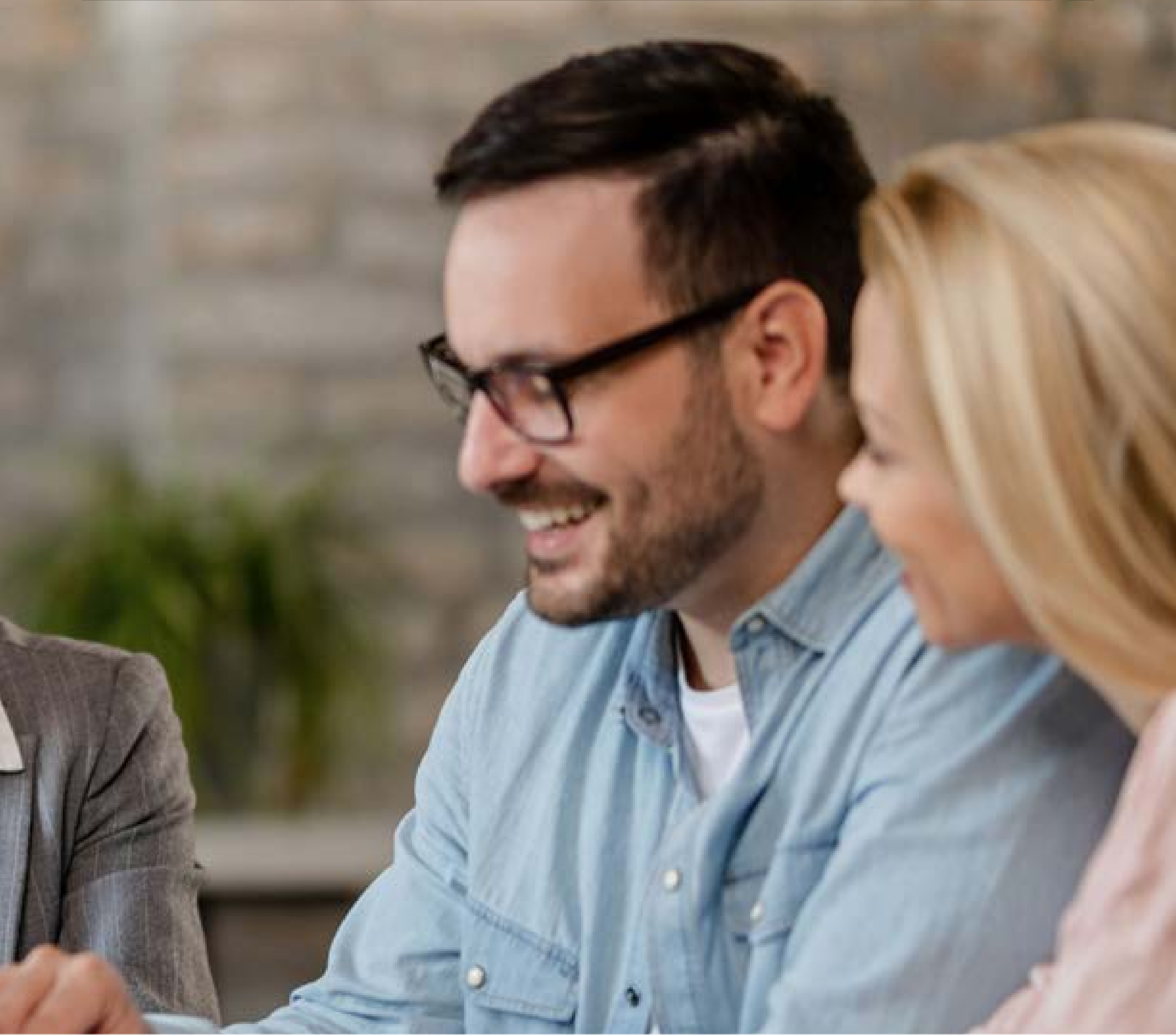
Compensation Strategy
Ensure the development of an executive compensation strategy that specifically defines where the organization will target each component of compensation for members of the executive leadership team.

Overall Strategic Planning
Ensure the strategic plan clearly defines how the bank will position itself in response to economic trends and changes in the banking industry.

CECL/Incentive Compensation Plan Design
Develop a communication strategy for internal and external stakeholders that addresses the anticipated impact of CECL implementation on the ability of plan participants to achieve performance-based goals.

Turnover and Millennials
Implement a human resources strategy that addresses how to fill the talent pipeline for positions with high turnover rates, and develop compensation strategies that offer plan features valued by millennials such as flexible working schedules and student loan repayment programs.

Read How CECL Will Impact Incentive Compensation Plan Design for more information on trends affecting incentive compensation.



ABOUT BDO

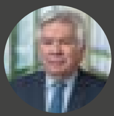
BDO is the brand name for BDO USA, LLP, a U.S. professional services firm providing assurance, tax, and advisory services to a wide range of publicly traded and privately held companies. For more than 100 years, BDO has provided quality service through the active involvement of experienced and committed professionals. The firm serves clients through more than 65 offices and over 700 independent alliance firm locations nationwide. As an independent Member Firm of BDO International Limited, BDO serves multi-national clients through a global network of more than 88,000 people working out of more than 1,600 offices across 167 countries and territories.

BDO USA, LLP, a Delaware limited liability partnership, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms. BDO is the brand name for the BDO network and for each of the BDO Member Firms. For more information please visit: www.bdo.com.

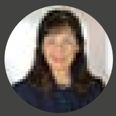
Contact Us

If you have any questions, comments or suggestions, please contact our Compensation Consulting practice by emailing us at compensation@bdo.com or by calling your local BDO office.

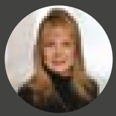
THE BDO 600 STUDY TEAM CONTACTS:



TOM ZIEMBA
312-233-1888
tziemba@bdo.com



JUDY CANAVAN
215-636-5635
jcanavan@bdo.com



KRISTEN KOSTNER
314-655-6236
kkostner@bdo.com

FIRST NAME

LAST NAME

EMAIL

PHONE

SUBJECT

MESSAGE

SUBMIT

Material discussed is meant to provide general information and should not be acted on without professional advice tailored to your firm's individual needs. To ensure compliance with Treasury Department regulations, we wish to inform you that any tax advice that may be contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding tax-related penalties under the Internal Revenue Code or applicable state or local tax or (ii) promoting, marketing or recommending to another party any tax-related matters addressed herein.