Tipping the Balance

Collective Action by Finance Workers Creates »Regulation From Below«

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September 2018

- Ten years after the last big financial crisis, major players in the global financial sector continue to dominate markets, neutralize regulation and jeopardize economies with illicit, reckless and sometimes illegal financial practices.

- Debates abound over regulatory oversight of large banks and the best methods of safeguarding consumers and economies, yet little attention has been paid to the role that the nearly eight million commercial bank employees in the global banking sector might play to foster better banking practices.

- Instead of relying on legal and supervisory systems to take on the entire task of financial regulation »from above«, the authors argue that employees of banks and financial institutions can collectively assist regulatory efforts »from below« and, in doing so, build safeguards for their own jobs against the incentivization of excessive or fraudulent sales, while at the same time helping to create a more stable and sustainable global financial system.

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Introduction

This paper examines the value of engaging finance workers in efforts to manage risk in the global financial sector. Regulators and management both continue to struggle to sufficiently oversee and mitigate risk in large and highly complex financial institutions. As explored here, empowered and organized finance workers can create a form of »regulation from below« that substantially aids and augments risk management in the financial sector. This paper will focus on the particularly acute need for »regulation from below« in the United States (U.S.) context and will highlight successful examples in other countries. Firm managers and directors, as well as policy makers at all levels, should consider this model as an important component of a policy framework to strengthen risk management in the financial sector and the economy more broadly.

In recent several decades the financial sector has expanded rapidly. Complex and risky financial products have driven profitability in the financial sector while leaving the real economy—that is, the part of the economy concerned with the actual production of goods and services—overleveraged, undercapitalized, and increasingly unstable. The market failure of 2008 demonstrated that in the absence of effective regulation or countervailing forces, the financial sector will prioritize short-term gains over long-term growth and stability. The consequences of this failure were borne largely by people who lost jobs, retirement savings, and the stability and security of their homes (Johnson and Kwak, 2010).

Ten years after the crisis, the need for »regulation from below« has, if anything, grown, with the world's largest banks, including the U.S.'s »big six.«[1] These financial institutions are larger, less safe, and more volatile than ever, according to market conditions (Sarin and Summers, 2016). Moreover, legislation and prudential regulation established to safeguard economic stability after the economic crisis is being weakened or repealed (Tracy and Ackerman, 2018). Once again, conventional regulation seems to be unable to constrain risky bank conduct that is not only undesirable for the banks, but also for their employees, customers, shareholders, and the economy as a whole (Egan, 2016).

1. The »big six« are Wells Fargo, Bank of America, Citigroup, JPMorgan Chase, Goldman Sachs, and Morgan Stanley.

Two case studies from the U.S. demonstrate these points: the Wells Fargo fake accounts scandals and Santander's aggressive sales of subprime loans. In both cases, the senior management of these mega-banks imposed abusive sales goals and incentive compensation arrangements on their employees. Yet in both cases, workers, in the face of great resistance, were instrumental in bringing the wrongdoing to light, first to the firm itself and later to regulators. Both examples, however, illustrate that engaging and empowering workers could have aided in detecting and addressing these risks much earlier. In the case of Wells Fargo, employees had been bringing concerns over sales goals to the attention of management for years before any action was taken, and consumers were harmed as a result of this inaction.

A third example demonstrates how this idea of regulation from below may well have benefits beyond the U.S. Constant restructurings and downsizings, some of them the direct result of the economic crisis, continue to shape the working lives and well-being of bank employees. Bank workers experience the effects of deregulation and emerging technologies through new types of jobs. Work-related stress in banking is now at critical levels, with negative effects on workers' health and thus also on their firms (Giogi, Arcangeli and Perminiene, 2017). Negative well-being lowers the productivity and efficiency of employees and compromises customer service. Unions can decrease »job strain,« and in turn increase workers' productivity, by affording them more control, autonomy, and support on the job (Karasek, 1979, Landsbergis and Cahill, 1994, and Dollard et al., 2000). The quality of jobs determines workers' productivity and their contribution to sustainable economic performance (Cazes, Hijzen and Saint-Martin, 2015, and SSF Stiglitz et al., 2009).

An organized workforce capable of wielding power through collective bargaining in the banking sector can be an important tool for systemic risk management in the financial sector. There are several structural reasons for this. First, line workers in banking have interests and compensation structures different from those of senior management and directors—whose interests are increasingly bound to the interests of short-term equity holders rather than to the long-term interests of the bank and its shareholders. Second, the ability to bargain collectively on compensation limits the ability of the firm to push aggressive and risky products through its sales team. Additionally, when workers have greater autonomy and control over their working conditions, »job strain« is reduced and productivity is increased (Karasek, 1979). Third, the protections and structure of a union allow workers to raise concerns, take the initiative, and share their valuable experience without fear of retaliation. The combined assets and employment footprint of large banks in the U.S. suggests that even changes by individual institutions could have powerful knock-on effects, both in the financial sector and in the wider economy.

Unions are already functional partners in the management of the financial sector in economies around the world. The international examples offered here show that unions act as a countervailing force against the negative effects of financialization and have bolstered the resilience and stability of their domestic financial systems. In continental Europe, employees and unions from country operations sit on European Works Councils (EWCs) and frequently consult with senior management. »Employees often have hands-on problems and challenges in the daily work in the [banks], which can gain from this information when planning changes« (IF Union Team, Union in Nordea and Danske Unions, 2008). The model of co-determination used in Europe, and most well-known in Germany, is correlated with improved firm performance as well as with stronger macroeconomic indicators. Research on the labor market in Argentina demonstrates that strong labor institutions support macroeconomic stability. In spite of these successes, the U.S. remains an outlier among advanced economies in that nearly all employees lack an independent worker voice in the financial sector (A. DiCristo, personal communication to author, 22 February 2018).

This paper will begin by examining the context for »regulation from below«—financialization and its impact on the broader economy. The second section will consider the financial sector in the U.S. specifically, including the role of deregulation and persistent risks in banks' operations. Two case studies will illustrate both the nature of the risks and the role that workers have played in addressing them. The third section describes the structural benefits and benefits for transparency of a unionized workforce. The fourth section walks through several international examples of how collective action and incorporating worker voices into corporate governance have supported risk mitigation in financial firms, the financial sector as a whole, and the broader domestic economy – creating a form of »regulation from below.«

The final section will conclude and offer a set of policy recommendations for firms and policy makers at all levels to support bank workers in creating useful »regulation from below.«

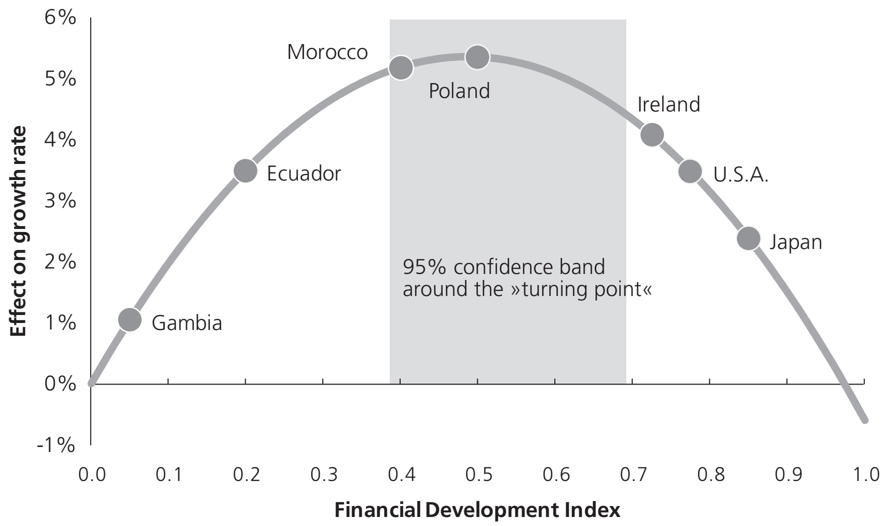
Section 1: Financialization and the Global Economy

Trends in the global economy since the 1970s have been characterized by a marked increase in economic instability and inequality. We have experienced more intense boom-bust economic cycles and disturbing long-term microeconomic trends such as crumbling public infrastructure, bankrupt municipalities, and growing retirement insecurity for young and old generations alike (Gillers, Tergeson and Scism, 2018, and Morrissey, 2016). These dynamics culminated in the Great Recession of 2008, when tens of millions of people around the world lost jobs, retirement savings, and both the value and stability of their homes. The roots of these developments can be found in neoliberal ideology and the trend of financialization to which it gave birth.

Financialization is the increasing role of financial motives, financial markets, financial actors, and financial institutions in the operation of economies (Epstein, 2005). In the 1980s, the role of the financial sector grew in most advanced economies. In English-speaking countries the dominant form of corporate governance shifted toward increasing shareholder value and »short-termism.« Dividend payments to shareholders rose along with top management salaries. Business strategies that sought to generate profits by taking more financial risk increased in scale and scope, including hostile takeovers, mergers and acquisitions, and leveraged buyouts. Employment opportunities suffered, as strategies to contain the costs of human capital became core principles of corporations: downsizing, outsourcing, eliminating pensions, reducing benefits, and decreasing wages (Hein, 2013).

The result was that, in advanced economies, financialization helped drive acute wealth inequality (Kus, 2012), increased macroeconomic risk, and market volatility (Stiglitz, 2015, and Arcand, Berkes and Panizza, 2012) and, ultimately, fed a cycle that led to more financialization (Kumhof and Ranciere, 2010). As wages have lagged for decades in some advanced economies, aggregate demand has been weakened (Stockhammer, 2013). De-

Figure 1. The Effect of Financial Development on Growth



Source: IMF staff estimates (Sahay et al., 2015).

mand—and workers' standards of living—have instead been propped up by access to cheap credit, via low interest rates, deregulation, and riskier financial products.

These trends suggest that, absent new models for reining in its power, the financial sector will continue to expand and consolidate, significantly diminishing the ability of governmental institutions to withstand pressures to deregulate and the ability of workers to bargain over wages. The cycle is continued as this leads to even further financialization and destabilization of the economy as a whole (Kumhof and Ranciere, 2010, and Stiglitz, 2015). Inequality will also continue to grow. An initial regression of financialization indicators and income inequality—controlling for conventional explanations of inequality—has shown a high correlation between the two (Kus, 2012).

Ironically, the very people whom the Anglo-American corporate governance model is supposed to place in control, long-term shareholders, are also ultimately harmed by these trends. Even as the »shareholder primacy«[2] model of corporate governance has become predominant, the risks it has created for workers, consumers, and the economy have spilled over to affect shareholder value. The Wells Fargo case study examined below provides a clear example of this trend. The bank's aggressive pursuit of market share through »cross-selling« created an uncontrolled risk for the bank's customers and workers—from line bank workers selling credit card accounts to professional wealth managers and advisers (Reuters, 2018). When these risks manifested themselves, shareholders lost share value and, through the disruption to the corporate structure that ensued, Wells Fargo lost its CEO, experienced an almost complete turnover of its Board of Directors,[3] and had serious restrictions placed on its growth (Flitter, Appelbaum, and Cowley, 2018).

Research by the International Monetary Fund (IMF) found a »tipping point« in financial development beyond which the risks of increasing financialization outweigh the benefits to overall economic growth. »Too much finance,« i.e., when credit to the private sector reaches 80-100 per cent of GDP, increases macroeconomic volatility (Arcand et al., 2012). Total factor productivity[4] declines and inefficiencies are introduced when the financial sector expands past the tipping point. While capital *accumulation* remains unimpeded, capital allocation and the efficacy of corporate control begin to break down (Sahay et al.,

2. Shareholder primacy is a theory in corporate governance holding that shareholder interests should be assigned first priority relative to all other corporate stakeholders.

3. In 2017, Wells Fargo elected six new directors and a new independent chair. Only two directors have been part of the board since 2009; the remaining members were appointed in 2015 or later. *See:* https://www.wellsfargo.com/about/corporate/governance/.

4. Total factor productivity is the portion of output not explained by traditionally measured inputs of labor and capital used in production.

2015). The essential and functional role of the finance sector is compromised when it exceeds its appropriate share, and this causes negative externalities in society (Figure 1).

The IMF study identified certain regulatory principles that create an »enabling environment,« that is, one in which financial stability and financial growth are both promoted by effective regulation. Countries with regulatory regimes that most closely complied with the Basel Core Principles, the Insurance Core Principles, and the International Organization of Securities Commissions Principles have experienced little or no trade-off between financial growth and stability. Broadly speaking, these principles capture »(1) the ability of regulators to set and demand adjustments to capital, loan loss provisioning, and employee compensation; (2) regulatory definitions, such as definitions of capital, nonperforming loans, and loan losses; and (3) financial reporting and disclosures« (Sahay et al., 2015). The challenge however, is how to get from a political economy regime where financialization has undermined the »enabling environment« to a new and more stable equilibrium.

Instead, the current trajectory of deregulation in the U.S. undermines each of those three broad objectives. Legislation passed in the aftermath of the 2008 financial crisis has been altered to minimize disclosure requirements, limit the purview and enforcement abilities of regulators, and diminish bargaining power to negotiate over employee compensation. Furthermore, actors in the financial sector typically are able to innovate—i.e., exploit opportunities for regulatory arbitrage—far faster than regulators can regulate, thus broadly undermining the efficacy of financial regulation (Johnson and Kwak, 2010).

The banking sector helps accelerate financialization through its role in financing, underwriting, lending, and securitizing a larger and larger range of business transactions. These trends are connected with the fact that investment banking in particular tends to be highly concentrated. Five U.S. banks, JP Morgan Chase, Bank of America, Citigroup, Goldman Sachs, and Morgan Stanley, are estimated to control nearly 70 per cent of the global market (IBISWorld Global Investment Banking & Brokerage, 2017).

As a whole, the banking sector is also is highly effective at broadly using its strength to preserve its privilege, further confounding the challenge of effective regulation (Abernathy, Konzcal and Milani, 2016, and Bapuji, Husted, Lu, and Mir, 2018). The following section will consider the significance of banks in the U.S., their consolidation and role perpetuating some of the more destructive tendencies associated with financialization.

Section 2: The U.S. Banking System

The largest banks in the United States dominate the global economy. Almost one-third of the 30 global systemically important banks (G-SIBs) identified by the Financial Security Board (FSB) are located in the U.S. (Financial Security Board, 2017). Of these, six major financial firms (Wells Fargo, Bank of America, Citigroup, JPMorgan Chase, Goldman Sachs, and Morgan Stanley, »the big six«) have substantial control and market share in the industry.

These six companies collectively employ more than 1 million (exclusive of temporary, subcontracted, or third-party contracted) workers and hold more than 10 trillion U.S. dollars in assets, or more than 50 per cent of the U.S.'s annual GDP. Globally, there are more than 7 million people employed in commercial banking, suggesting that the precedent set by leading banks could affect a far broader segment of the world population (IBISWorld Global Commercial Banks, 2017).

The events of the financial and economic crisis that began in 2008 demonstrated that these financial institutions are so large and interconnected that their risk-taking behavior can have effects that extend far beyond their own shareholders and creditors. As a result, most commentators after the 2008 crisis have accepted the need for much more robust systemic regulation and have realized that the *governance* of these institutions was important systemically.

The financial sector is also responsible for exacerbating and perpetuating wealth inequality within its ranks (Jaumotte and Osorio, 2015). Citigroup and JPMorgan Chase both compete for the highest CEO-to-worker pay ratios at 369:1 and 364:1, respectively; the CEOs of the »big six« were paid more than $130 million U.S. dollars

Figure 2. Asset and Employment Footprint of the »Big Six«

	Global Assets	% U.S. GDP	Global Employment
JPMorgan Chase	$2.5 trillion	13%	243,355
Bank of America	$2.3 trillion	12%	224,000
Wells Fargo	$2.0 trillion	10%	269,000
Citi	$1.8 trillion	9%	219,000
Goldman Sachs	$916 billion	5%	34,400
Morgan Stanley	$852 billion	4%	55,802
Total	$10.4 trillion	52%	1,045,557

Sources: Information taken from S&P Global Intelligence, the U.S. Bureau of Economic Statistics, and banks' annual reports filed with the Securities and Exchange Commission (SEC).

in 2017 (AFL-CIO Paywatch, 2018).[5] The leaders of the industry—the »big six«—tend to be so powerful that one of these banks' operational decisions can help to set an industry standard.

The Challenge of Regulation

To understand the need for »regulation from below,« it is important to understand the structural obstacles to effective financial regulation. The predominance of »information asymmetries«[6] in the financial sector, the continuous evolution of complex financial products and transactions, and the strength of the financial lobby present significant challenges to effective financial regulation (Abernathy et al., 2016). While free market theory presumes that the market is self-correcting and able to regulate itself, the influence of the financial lobby in the U.S. and the absence of regulation there provide strong evidence that the real dynamics of financial regulation and financial market functioning are better understood through the lens of political economy. Financial institutions in 2009 had 25 times the number of lobbyists in the U.S. Capitol as their opposition (Johnson and Kwak, 2010).

The IMF found in 2009 that the lenders that lobbied in the U.S. most extensively in the lead-up to the crisis had several common characteristics: lax lending standards, a greater tendency to securitize, and faster-growing mortgage loan portfolios with higher delinquency rates—indicating that the firms lobbying before the crisis did so to obtain private benefits (Igan, 2009). Industry lobbying efforts consistently undermine state policies by supporting federal action to encourage deregulation and avoid oversight, while making nearly unrestricted financial contributions to electoral campaigns (Johnson and Kwak, 2010). In this context, regulation from below is a way of counterbalancing the political power of finance.

A series of major deregulatory changes in the last two decades demonstrates how this intersection of economic and political influence has led deregulation that turned out to be harmful to financial stability, growth, and shareholder value, among other things.

The Repeal of the Glass-Steagall Act in 1999

The Glass-Steagall Act was passed in 1933 in the wake of the Great Depression. The primary function of the act was to separate commercial banking (federally insured depository institutions) and investment banking (financial institutions engaged in speculative investing, including firms trading on their own account). This system supported financial stability and promoted access to credit for operating businesses for the better part of a century. Beginning in the 1980s, the financial sector began a sustained boom and grew from 16 per cent of domestic corporate profits to 41 per cent just before the crash in 2008 (Johnson, 2009). With this growth, the political power and risk appetite of the industry expanded (Johnson, 2009).

5. Wells $17,564,014, Citigroup $17,801,683, JPMC $28,313,787, Morgan Stanley $24,509,722, GS $21,995,266, Bank of America $21,779,832. Total: $131,964,304. *See*: https://aflcio.org/paywatch/highest-paid-ceos.

6. Asymmetric information, also known as information failure, occurs when one party to an economic transaction possesses greater material knowledge than the other party. This normally manifests itself when the seller of a good or service has greater knowledge than the buyer, although the reverse is also possible. Asymmetric information may lead to adverse selection or moral hazard, which are situations where individual economic decisions are hypothetically worse than they would have been had all parties, possessed more symmetrical information.

Over that period, the financial industry launched intensive lobbying efforts, leveraging a revolving door between banks and key government posts and growing campaign contributions to both major parties. This trajectory culminated in the merger of Citibank and Travelers Insurance in 1998. The law at the time allowed for a two- to five-year divestiture of nonbank holdings to comply with Glass-Steagall's separation of commercial and investment banking (Martin, 1998). Rather than divesting, however, then-Travelers CEO Sandy Weill began a major lobbying and public relations campaign to repeal the Glass-Steagall Act. Weill went to Congress with the support of President Clinton to urge members to act and promised a new »financial supermarket« that would be more efficient and deliver better prices and customer service. This put legislators in a position to accede or force the unwinding of the merger and stand in opposition to the latest financial innovation of the era (PBS, 2003).

When the Glass-Steagall Act was repealed, it was followed by significant merger and acquisition activity in the financial sector: 37 major financial institutions in 1990 merged into just four by 2009 (Mother Jones, 2010). This consolidation in large part gave rise to the »too big to fail« banks. After the crisis of 2008, Sandy Weill publicly reflected that the repeal of the Glass-Steagall Act was a mistake (Reilly, 2012).

The Ban on Regulation of Derivatives in 2000

Increasing activity in derivative contracts, another, related, driver of the market's failure in 2008, was made possible by the passage of the Commodities Futures Modernization Act (CFMA) in 2000 (Stout, 2011). The CFMA was included as part of a larger spending bill by Sen. Phil Gramm (R-Texas) with the support of the U.S. Treasury Department under Larry Summers, and was signed into law by President Clinton (Lipton, 2008). Passage of the CFMA allowed derivative and swap instruments to grow rapidly in the unsupervised and opaque »over-the-counter« marketplaces. The act created indirect demand for the purchase of risky mortgage-backed securities because it permitted investment banks to sell uncleared Collateralized Debt Obligations (CDOs) and Credit Default Swaps (CDSs) (Black, 2012). Hedge funds, for example, purchased CDSs as insurance while they bought junior tranches of risky mortgage-backed securities (Silvers and Slavkin, 2009). Although CDOs were meant to mitigate the risk of holding mortgages, and default swaps were meant to provide a hedge against nonperforming loans, when toxic mortgage assets began to collapse, both financial products magnified, rather than mitigated, the losses and thereby also the severity of the crisis (Gerding, 2011).

Although the crisis was followed by a partially successful effort to regulate these financial products, the derivatives market continued to grow. The provisions of the Dodd-Frank Act that sought to wall off the derivatives market from the commercial banking system were from the passage of the act the primary targets of new deregulatory efforts. According to a research report by Citigroup, synthetic CDOs were expected to grow to 100 billion U.S. dollars in 2017 from only 20 billion U.S. dollars in 2015 (Alloway, 2017). Other research shows that within a month of derivatives regulations being issued, industry groups had identified a loophole in a footnote and circulated a memo asserting the ability to trade derivatives through foreign subsidiaries in much the same fashion as they had if they were not referred to as »guaranteed« (Greenburger, 2018). Thus in spite of efforts to regulate, the riskiest segments of the market that drove the collapse of 2008 are still operating at a scale and in an interconnected manner that has negative implications for financial stability.

The »London Whale«

In addition to the clear challenges that the size and power of the financial industry poses to regulators, the scale of the largest financial institutions makes internal oversight and the creation and operation of effective internal controls by management and boards very difficult. The complexity of financial institutions has led to breakdowns in internal risk management, communications, oversight, and governance, earning them the label »too big to manage« (Birkinshaw and Heywood, 2009). The problem can be played out in highly specific and narrow instances like that of the »London Whale,« or in pervasive and longstanding company-wide practices like the accounts scandal at Wells Fargo (discussed in the next section). In both cases, shareholders and the firm lost significant value because of a failure of internal risk management.

In 2013, JPMorgan Chase paid more than 900 million U.S. dollars to four regulators in the U.S. and the United Kingdom, admitting that it had violated securities laws, in a scandal known as the »London Whale.« Bruno Iksil earned his nickname »the whale« by taking large positions in thinly traded markets that then became difficult to unwind. While working under the CIO of the bank, Iksil lost 6.2 billion U.S. dollars gambling on risky and complex financial instruments. The charges filed at the time indicated that the risks and losses taken by this group of traders were hidden from senior management. Later, however, Iksil went on record and indicated that senior management was aware of his trading and had directed him specifically to trade in that manner: »My role was to execute a trading strategy that had been initiated, approved, mandated and monitored by the CIO's senior management« (McNulty and Zuckerman, 2012). Whether the losses had been hidden *from* senior management or *by* senior management, the fact remains that there was a material breakdown in internal risk controls and corporate governance.

Workers' Role in Governance

The United States is an outlier in terms of the world's major open economies in its lack of an independent worker voice for bank workers. And, as the previous section illustrated, both regulators and banks in the U.S. have struggled to effectively oversee and manage risk in the financial sector. At the core of this oversight failure is the inability of financial institutions' boards of directors to provide a sufficient check on bad actors. At the same time, firms have been largely unable to »establish or maintain an effective broader workplace culture with appropriate risk governance and controls« (Heltman, 2018).

Bank employees, regardless of their status, often do not feel safe enough to speak up about misconduct. The CEO of Morgan Stanley, James Gorman, recognized that banks fall into the same »tyranny of success« as other companies and assume that because they have been doing business a certain way for a long time that it must be right. For example, Gorman pointed to the business practices associated with the mortgage securitization market and misleading products sales prior to the crisis (Broughton, 2018).

Given the intractability and seriousness of the challenges of risk management in the financial sector, policy makers should consider the role workers could play in corporate governance solutions if employees feel safe and supported when doing so. Workers are responsible for executing banks' day-to-day operations, and workplace conditions have a significant impact on workers' productivity. This in turn affects the efficiency, profitability, and integrity of a bank's operations. As the following examples illustrate, workers' firsthand experience engaging with consumers and conducting a firm's business can be an invaluable asset for regulators or the firm in managing risk. Bank workers are also at the nexus of those problems that can create systemic risk – increasing the volume of high-yield, high-speed sales in a struggle for more market share. When companies communicate changes poorly, when they set unrealistic sales expectations, and when they define employees' success in performance in this context, a union is the solution.

Wells Fargo

On 8 September 2016, the U.S. Consumer Financial Protection Bureau (CFPB) announced fines against Wells Fargo for opening millions of checking and savings accounts and credit cards in clients' names without their consent (CFPB, 2016). The bank paid out record-setting fines over the next several years in addition to entering into settlement and consent orders with regulators. In the wake of the scandal, Wells Fargo attempted to blame more than 5,300 workers for the fake accounts and fired them; however, further investigation revealed the scandal was driven by a poor corporate culture and coercive incentive pay structures (Rucker, 2017).

With more commercial banking market share than any other U.S. bank, Wells Fargo sought to expand profitability by adopting a »cross-selling« strategy called the »Gr-eight Initiative« (D'Acosta, 2017). The initiative set an internal goal for employees of selling at least eight financial products to each customer and connected incentive compensation to this goal. One worker has explained that her base pay was approximately 45,000 U.S. dollars annually but could reach 81,000 U.S. dollars annually if she met all of her goals (Anonymous employee, personal communication to author, 1 May 2018). It is important to note that a living wage for an individual in San Francisco supporting one child, for example, is estimated to be more than 80,000 U.S. dollars a year (MIT Living Wage Calculator, 2018).

»Banking on the Hard Sell«, a report by the Committee for Better Banks and the National Employment Law Project, examined »the use of aggressive sales metrics and incentives programs to encourage frontline workers to push multiple banking ›solutions‹, or products, on unwitting customers.« It concluded that low base pay, aggressive sales metrics, and performance incentive pay were creating not only hostile working conditions for employees, but also forcing them to choose between questionable sales practices and making ends meet (Christman, 2016).

In spite of this, workers persisted in raising these issues with the firm and regulators for years.

More than a year before the scandal broke; more than 20,000 Wells Fargo workers signed a petition calling for an end to the aggressive sales goals and performance pay systems. Workers raised the same demands in 2014 and 2015 at Wells Fargo's annual shareholder meetings. Without any movement from the company in response, workers eventually took direct action, occupying the lobbies of Wells Fargo buildings in Los Angeles and Minneapolis. Workers also came to Washington, D.C., to brief members of Congress, the CFPB, and the Office of Comptroller and Currency (OCC), which led to meaningful enforcement action.

Workers' efforts yielded important changes at Wells Fargo and in the industry as a whole. Following the CFPB's enforcement action, Wells Fargo announced that it would eliminate sales goals nationally. Additionally, the bank established a Stakeholder Advisory Council, which includes representatives from state pension funds, faith-based investors, community organizations, environmental groups, and others. Organized workers, however, have not been included and continue to seek a formal seat on the council.

At JPMorgan Chase, incentive pay structures appear to be similarly perilous. A worker reported a base salary of 33,000 U.S. dollars that in the past could have reached 71,000 U.S. dollars with incentives (Anonymous employee, personal communication to author, 3 May 2018). Following the Wells Fargo action, CEO Jamie Dimon announced a wage increase for 18,000 of the lowest-paid employees of the bank, which moved the wage floor from 10.15 U.S. dollars an hour to a range of 12 to 16.50 U.S. dollars an hour (Reuters, 2016). Finally, the Los Angeles City Council passed a Responsible Banking Ordinance in June 2018 to reform the city's bank contracting process by requiring whistleblower protections for workers and the disclosure of sales goals (Reyes, 2017, and Wack, 2017).

The Wells Fargo case demonstrates that workers can play an important role in recognizing and managing risk in financial institutions. The scandal was ultimately a huge expense for the bank, its managers, their shareholders, consumers, and employees. Workers, however, sounded the alarm early. Had the governance of the bank been structured to listen to them, all parties may have been spared some of this expense.

Santander

The Spanish bank Santander entered the U.S. subprime auto lending space in the early 2000s. With investment from private equity, it grew that unit into the public company Santander Consumer USA, which is now one of the largest subprime auto lenders and securitizers in the U.S. (Massoudi and Rodrigues, 2014). Santander's business practices from the time of its entry into this market have raised serious issues involving false statements and conflicts of interest reminiscent of the pre-2008 subprime mortgage market. The majority of Santander's loans are originated through complex and opaque indirect relationships with auto dealerships, and Santander has maintained profitability by developing specialized methods of collecting on defaulted auto loans. The dealerships concerned would routinely falsify or inflate borrowers' incomes. The banks involved would then resell those loans to investors, knowing they were unsafe (Fernandes, 2017). As Massachusetts Attorney General Maura Healey stated in the wake of a settlement with the bank, for Santander »the global economic collapse wasn't a cautionary tale. It was a blueprint.« (Saunders, 2017).

Here, as in the case of Wells Fargo, workers raised many risks and concerns regarding Santander's practices. Workers noted instances of Santander Consumer customers' loans being extended without any contact with the customer and identified the high-pressure environment at call centers and business practices that created a dangerous cycle of defaulted and reinstated loans potentially harming hundreds of thousands of consumers (McGrath, Christman, and Keyser, 2017). They also alleged the company's performance monitoring and incentive system impeded their ability to speak up about practices that might harm customers and pressured them to approve loans too quickly and to collect on debt in unsavory ways. Workers identified that the new speech recognition and call quality monitoring software, »CallMiner,« had a potentially discriminatory impact on their performance scores (McGrath et al., 2017).

Workers also participated in the company's annual general meeting, with one worker, Jerry Robinson, explaining:

> »When I was an employee in the Reinstatement Department, our performance was evaluated on metrics that included the number of delinquent loans we could successfully reinstate. If we failed to reinstate loans, it could result in no bonus, possible disciplinary action, and even termination. Our managers said our job was to try to get customers back in their cars, even if they had defaulted on their loans and had their vehicles repossessed. They said we had to try to reinstate the loan, get the customer to pay the repossession fees, take the past due months' payments, and put them on the back end of the note and charge these customers another modification fee. Our job was to get people who were already upside down on their loans back in their cars by making them pay more fees. This was a cycle that customers could repeat several times over the life of their loan, and it became clear to me that this cycle of defaults, and loan reinstatements, was NOT in the best interests of our customers«.

Finally, workers from Santander also briefed members of Congress, the CFPB, and the OCC in 2016 and 2017. In spite of the risk of retaliation, they detailed practices like being directed to *not* fully explain the company's Guaranteed Asset Protection (GAP) insurance policy to customers (a key part of their add-on product marketing that would not fully cover potential customer losses) as well as several of the issues described above.

Again, workers' efforts led to meaningful action. The CFPB levied a fine of 10 million U.S. dollars on Santander for deceptively marketing so-called overdraft protection and signing up customers for the product without their consent in 2017. Members of Congress also wrote to Santander about the potentially discriminatory impact of »CallMiner.« A few months later Santander restructured its performance monitoring and incentive system and eliminated the use of »CallMiner« in performance measurements (Hoffman, 2017).

At Santander, as in the Wells Fargo case, workers worked together to raise concerns about risky practices by their employer. In both cases, the practices were harmful to multiple stakeholders, including the firm, its shareholders, and its customers. Workers provided early warnings about problems that were not previously identified or addressed by internal risk management controls or by external regulators, organically forming a type of »regulation from below.«

These two cases show how in the U.S., even in the context of workers being particularly vulnerable, the model of »regulation from below« has had real successes. These successes suggest that if supported properly, this model could contribute to a structural solution to risk management in the U.S. financial sector. The next section will consider the potential and requirements of such a model.

Section 3: Organized Bank Workers as a Solution

Bank workers bring important experience and perspective to the challenge of risk management in the financial sector. However, to engage workers effectively in »regulation from below,« stability and structural support are required. This section proposes that bank workers' unions can provide the structure necessary for such a model to succeed.

As discussed above, the rise of financialization has led to a weakening of external controls and a growth in risk-taking behavior. This results in high-risk products designed to increase yield and aggressive sales tactics designed to increase market share. Workers often find themselves at the intersection of these two trends.

Unions bargain over issues that affect their members, like the workplace conditions and aggressive sales tactics described above, in addition to adequate staffing, employment inclusivity, the establishment of a labor-management committees, and the more traditional issues of compensation, benefits, and overtime or merit pay (Professional Employees, 2017). Unions representing a wide range of workers in the U.S. have been highly effective in accomplishing similar issues in their own fields. One particularly relevant example is collective bargaining in health care, where doctors, nurses, and health care workers have negotiated directly with hospitals to improve nurse-to-patient ratios and the quality of care provided. These unions have also provided valuable insight in the political debates around health care.

Furthermore, as international examples illustrate (discussed in detail below), unionized workers can make important contributions to industry-level conversations about financial regulation and policy. Countries with strong labor laws and institutions have seen these structures act as a countervailing force against the trend of financialization. This section will examine how an organized workforce can contribute to both firm and systemic risk management through the ways in which bank worker interests balance the equity-driven interests of management. This section also looks at the broad benefits of bargaining over wages, and the transparency and oversight workers can provide.

Bank Workers' Alignment of Interests

Since the financial crisis, there has been increasing attention by both regulators and researchers paid to the problems associated with equity-based compensation in financial institutions. Scholars such as Harvard Law School Prof. Lucien Bebcuck have asked whether it is really in the public interest for the executives of megabanks to have their compensation linked to short-term equity prices. The risk asymmetries and time horizon issues are well known to students of executive compensation. By contrast, while line bank workers and their unions definitely have their own interests, these interests are not subject to the same conflicts traditionally faced by senior management and boards of directors.

The consequence of management receiving short- to medium-term equity compensation is typically an excessive managerial focus on short-term stock price movements. Another common example is managers who pursue »empire building« rather than internal development, because CEOs are often compensated on the basis of the size of the firm. Although boards are tasked with overseeing management, key executives themselves often serve on the board, in some cases even as chair of the board. Even independent directors can become too complacent and lose track of their obligations to the corporation and its long-term shareholders. These problems are compounded by the fact that directors rely heavily on senior management for their information about the firm. Additionally, middle and senior management often lack incentives to report bad news up the chain of command, and instead demonstrate a strong bias to report only good news (Broughton, 2018). In the U.S., managerial employees have very weak protections in cases of higher-level wrongdoing.

On the other hand, the nonsupervisory workforce tends to be more concerned with the long-term stability of the firm, particularly when, as is typical, the bulk of its compensation is in the form of a traditional paycheck. In addition, the workforce tends to be, when given a real choice, more reluctant to cut corners in pursuit of profit maximization than managers with large stock option packages. With the protection of a union, workers can safely report questionable practices and potential legal violations, and flag potential problems, especially in working environments where there are bad working conditions and poor pay. A grievance procedure affords workers due process and dispute mechanisms, should retaliation occur. Even more importantly, pressure to engage in questionable or even fraudulent practices can be directly challenged with protection from discipline or termination.

Traditional economic analysis regarding unionized workers in the financial sector has focused on three primary (negative) impacts: (1) increased wages leading to diminished returns to shareholders and an increase in the cost of finance; (2) an alignment of interests with management with respect to »empire building«; and (3) a resistance to innovation. However, the combination of the role of equity incentives in the 2008 financial collapse and the role of sales goals and incentive pay in the Wells-Fargo scandal suggest that this traditional view is missing the mark, and that in particular it misses the question of the role that collective bargaining and protections against retaliation can play in shaping the overall behavior of financial institutions as regulated entities.

Bargaining Over Compensation

The ability to bargain collectively over compensation is a core component of union representation. As illustrated by the Wells Fargo case study above, coercive performance incentives can pose serious risks to the firm, workers, consumers, and shareholder value. Some bank workers interviewed recently have reported receiving up to half their annual income in the form of incentives—creating a disturbing dynamic in which workers were forced to choose between providing high-quality and responsible service to their customers and making ends meet for their own families. Yet it appears compensation for many U.S. bank workers is still supplemented with potentially perverse incentives. Recent interviews with bank workers in the U.S. suggest significant instability with regard to compensation and incentive payment systems overall (Christman, 2018).

Through formal labor relations, unions negotiate fair and equitable payment systems. Collective agreements generally increase and stabilize base pay, which can reduce dependence on incentives. Unions can bargain to limit the use of the sales goals, performance metrics, and incentive pay that workers say are harmful to customers and impede workers' ability to provide high-quality customer service. Increasing wages at the bottom of the pay scale has a high probability of reining in compensation at the top of the pay scale. Given quickly growing pay disparities between CEO compensation and the median worker salary in the financial sector relative to the rest of the economy, bargaining to correct these distortions could have an ameliorative knock-on effect across the whole economy.

When examining labor market institutions' impact on inequality, IMF staff found that an increase in union density reduces the top 10 per cent income share in the whole economy. The finding held true even when the results were controlled for the role of employment and compensation growth in the finance sector.[7] Within the banking sector, the absence of collective bargaining has had the consequence of allowing, for example, disproportional increases in executive compensation, while workers' remuneration remains largely stagnant, driving inequality, and excessive executive compensation at the top of the pay scale (Jaumotte and Osorio, 2015).

7. Compensation in the finance sector has grown fast relative to the rest of the economy; therefore the study was controlled for the share of hours worked in finance relative to the total economy.

Worker Voice and Transparency

Nonsupervisory bank workers often find themselves at the confluence of two main drivers of systemic risk: the acceleration of high-risk borrowing and lending, and the expansion of the volume of financial transactions. As a result, workers have particular insights into how financialization intersects with consumers and the real economy. The question is: do they have any way of (1) communicating those insights and (2) participating in processes that can make meaningful change based on those insights?

Bank workers with the protection and structure of a union can more easily report questionable banking practices, structural conflicts of interest, and other problems either to regulators or to the company itself. Without such protection and structure, workers lack the confidence to speak up, are vulnerable to retaliation, or will simply be ignored. Beyond early risk detection, nonsupervisory bank workers are often in a position to offer useful perspectives on larger business trends and bank regulation. The next section considers examples around the world where this has been the case.

The Worker Stress/Productivity Trade-off

Financial firms are fundamentally service-based businesses. Bank workers are often the primary, if not only, point of contact between a firm and its customers. As such, banks depend heavily on their workers as a primary source of value creation. Corporate operations and practices that lead to excessive worker strain or otherwise undermine the wellbeing of their staff are at odds with a focus on value creation. Unions, however, have strong incentives to bargain over workplace conditions that support the well-being of their members. Aggressive and risky bank practices are highly correlated with worker stress, which in turn corresponds to broader operational risks.

Intense competition in the financial sector has driven pressure to restructure and downsize as well as implement increasingly aggressive sales tactics and risky products. The diversification of services that came with industry consolidation led banks to transfer services increasingly to customer control (e.g., home banking). Bank employees' functions were therefore redefined, becoming something closer to »bank sellers« (Giogi, et al., 2017). As »bank sellers«, employees have goals for selling products as well as metrics that score both their pace and success in generating income from origination, servicing, and collections (Adrian and Ashcraft, 2016, and McGrath, et al., 2017). These trends are correlated with a sharp increase in work-related stress, which can diminish workers' and organizations' psychological and physical health (Giogi et al., 2017).

An anecdote from Wells Fargo demonstrates this correlation. Due to productivity, loyalty, and other metrics tied to incentive pay, Employee A in the Wealth Division faces incredible pressure, in general, to close complicated, nonconforming mortgages. Employee A has been deterred from renewing a notary certification, after witnessing Employee B's experience of receiving an excessive caseload because they could complete deals requiring review by a certified employee. Employee B's excessive caseload in a high pressure environment led to lawsuits over foreclosure, which placed an extraordinary burden on Employee B. Witnessing this colleague's distress, Employee A did not renew their notary certification out of fear Wells Fargo would continue to lack the internal controls necessary to allow for an employee to review a case with the amount of time necessary. Employee A reports extremely high levels of stress that cause migraines, hair loss, severe anxiety, and depression (Anonymous employee, personal communication to author, 30 May 2018).

An example from Italy is also instructive. The Italian banking sector has seen significant merger and acquisition activity over recent years, creating high risks for worker stress (Manocci et al., 2018). A 2017 study evaluating the stress level of bank employees found that 64 per cent felt the pressure to sell was in conflict with what they believed to be morally correct (Manocci et al., 2018).[8] Italian unions have been actively engaging major banks on these issues; at UniCredit Group, its European Works Council (EWC) has engaged with management on core issues regarding risk mitigation in the banking sector, responsible sales, and, most recently, a three-year proactive plan to deal with restructuring and reorganization.

8. Additionally, one quarter fell into the »distress« range of the results, 82 per cent were anxious about the failure to meet goals, and 84 per cent were uncomfortable recommending a product to customers just because it was in their »budget goal.«

Section 4: International Examples of Workers as Allies

In economies around the world, employers in the financial sector consult and negotiate with workers' organized representatives. Base pay is set by national or sectoral-level agreements in Europe, while in emerging countries in South America wages often are set in firm-level negotiations. Collective agreements provide bank employees with some control over their workload and notice, plus a potential voice in large-scale changes, together with the autonomy to take the initiative and speak up when they deem it necessary. This acts as a check on some major drivers of risk without sacrificing the profitability or expansion plans of their employers. At a broader level, unions play a practical, but little recognized role, in addressing some of the power imbalances associated with financialization.

The value of unions as a countervailing force is perhaps most observable in continental Europe, where labor relations are rooted in history and social norms. Collective bargaining coverage in the banking sector varies, but out of 23 countries assessed in 2011, 16 reported coverage rates of 80 per cent or higher (Eurofound, 2014). As a result, bank workers and their unions are very much part of the larger process of a social dialogue in which employees' representatives meet with governmental bodies and bank employer or industry associations. In these settings a wide range of workplace issues can be jointly raised, discussed, studied, and addressed. At a multilateral level, through organizations like UNI Global Union, the global union federation representing bank workers, and the International Trade Union Confederation, bank workers and their unions interact with multilateral institutions like the FSB and the IMF.

The experience of bank workers in Europe contrasts with banks' approach to employee relations in the U.S. The absence of collective bargaining in the U.S. has created a problem that is recognized at the highest management levels of banks (Broughton, 2018). As a matter of course, banks headquartered abroad bargain with their workers' unions in their home country. These bargaining relationships facilitate problem resolution and labor peace. But in the U.S. these same »foreign« banks ignore or oppose the efforts of employees to form and join unions, even though multiple stakeholders, such as consumers, shareholders, and governmental agencies could benefit from positive labor relations. For example, Banco Santander employees are represented by unions in Argentina, Brazil, Chile, Germany, Italy, Mexico, Poland, Portugal, Spain, and the United Kingdom. These unions have recognized the importance of extending labor relations to the U.S. and have publicly supported their colleagues' efforts to organize. Santander Holdings USA, however, continues to oppose its workers' efforts to form a union and to avail itself of all the tools available under U.S. labor law to frustrate those efforts.

The remainder of this section examines several diverse international examples, through the lens of how collective action, representation, and negotiation has supported a model of »regulation from below.«

Brazil: Bargaining for Equality and Productivity

There are several hundred thousand unionized bank workers in Brazil, whose unions continue to raise the important problems that bank workers are facing in the industry. Just like workers in many countries around the world, working conditions in the banking sector in Brazil are such that employees have intense demands on them while employees have minimal workplace control. Brazilian bank workers were twice as likely to experience mental health problems such as depression and anxiety based on the job strain model (Karasek, 1979). This was especially true where workers felt overcommitted, lacked social support at work, and there was in imbalance between their efforts and rewards (Silva and Barreto, 2010, and Petarli et al., 2015).

Brazil's leading labor confederation, and its finance federation, the CONTRAF-CUT, organizes to challenge these degrading working conditions. For example, the union signed an agreement to curtail harmful workplace practices with Banco Santander, a dominant bank in Brazil. In this agreement, the bank pledges to limit the use of unrealistic sales goals and public employee performance rankings. There is a joint recognition that responsible customer service is meaningful to a safer and sounder bank (A. DiCristo, personal communication to author, 3 May 2018).

Unions in Brazil's banking sector continue to mobilize to challenge acute inequality: in 2017, Brazilian bank employees challenged attempts by the National Banking Federation (Febraban) to undercut wages, and struck for 31 days when Febraban refused to apply pay raises. This was the unions' longest strike since 2004. Collectively, workers won an annual wage increase of 8 per cent, and food and child care allowance raises of 10 per cent and 15 per cent, respectively (Reuters, 2016).

Consultation and Communication

In addition to numerous local and national regulations and union structures, workers and employers in the EU and the European Economic Area (EEA)[9] have the right to establish European Works Councils (EWCs) at firms with at least 1,000 employees in two EU countries, or firms with at least 150 employees in the EEA. Each European Works Council is adapted to the companies and geographies where workers reside. EWCs are inclusive of worker, union, and manager representatives and have three basic functions: *information, consultation,* and *participation* (European Commission, 2018).

EWCs offer one potential template for the structure of »regulation from below« by providing workers an avenue to engage in dialogue with employers, governments, and employer or industry associations. These consultations can provide great benefits to regulators and the firm, as described in the Nordic context below. Consultation of this variety may restrain some of the more excessive compensation practices that are driving acute inequality, according to an IMF study. Strong trade unions may limit rent extraction and restrain some of the most excessive earnings tendencies in the financial sector (Jaumotte and Osorio, 2015).

The Nordic Model

The »Nordic model« represents one of the best uses of EWCs. Bank unions across Scandinavia—including finance unions from the IF (Insurance), Nordea Bank and Danske Group Bank—came together to form the Nordic Financial Unions (NFU) decades ago to ensure their EWC

9. Countries that are members of the EEA, but not part of the European Union, include Norway, Iceland, and Liechtenstein. Switzerland is in neither the EU nor the EEA.

structures would be used as effectively as possible and ensure a role for employees' comments and perspectives. The model is marked by »good cooperation between unions and management« and a high degree of trust between institutions (IF Union Team et al., 2008, and Blanchard et al., 2013).

The Nordic Financial Unions are highly organized. Unions train EWC representatives to support effective and useful meetings with the employer: simply put, »the employees often have hands-on problems and challenges in the daily work in the company, and the employer can gain from this information when planning changes.« The NFU also has established team structures to handle communications with national member unions, who in turn handle communication with individual members. At Nordea, IF and Danske Group, the NFU unions have created many additional structures in which employees meet regularly with HR, management in business segments, CEOs, among others, to facilitate the wellbeing of both employees and the firm. (IF Union Team et al., 2008).

Finally, the NFU is one of the most active participants in the European Sectoral Social dialogues on »Banks and Insurance« (A. DiCristo, personal communication to author, 3 May 2018). As an active stakeholder in banks at the EU level, the NFU has incorporated a new diversity of perspective in several EU financial regulations. Thus the NFU has successfully enabled communication within, between, and beyond financial firms—from nonsupervisory workers to senior management to national and regional regulators—in a way that would not have been possible without the structure of the participating unions. This kind of communication invites innovative solutions to the challenges of risk management in the financial sector.

Germany and Co-Determination

Germany is well known for co-determination in its corporate structure, which allows employees to sit on supervisory boards at major companies. Evidence suggests that introducing a worker perspective into corporate governance in this way has driven strong and sustainable business performance as well as macroeconomic benefits.

The Mitbestimmungsindex (Co-determination Index) shows that companies with board level co-determination have higher rates of reinvestment, including in worker training. It also shows that those companies' executive compensation practices are more oriented towards long-term objectives (Hans-Böckler-Foundation, 2018). Additional research has found that companies with a strong worker voice (i.e., board-level employee representation and coverage with collective bargaining agreements) show better performance compared with those without: they have higher market value and higher net sales, as well as higher productivity (Hassel and Helmerich, 2017, and Hans-Böckler-Foundation, 2018). Finally, companies with a union presence have resisted low (wage) price competition; instead, higher wages were achieved through increased productivity, which in turn made companies more competitive (Hans-Böckler-Foundation, 2018).

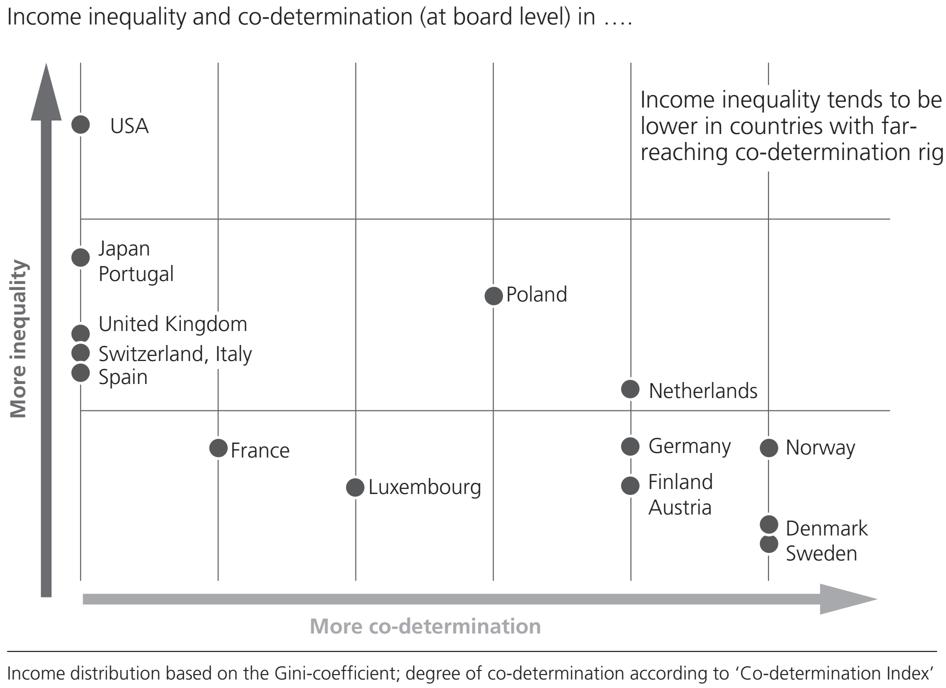
Co-determination is also linked to broader benefits for firms. Countries with strong worker representation in the corporate structure have higher overall investment in research and development (ETUI, 2016, and Hans-Böckler Foundation, 2018). Germany has also experienced a lower level of job loss because of the features of collective and company agreements. Finally, there is a strong negative correlation between co-determination and income inequality, as the following chart illustrates (Hans-Böckler Foundation, 2018).

Although Germany's Deutsche Bank is often raised as a counterexample against the merits of »regulation from below,« in part because of its role in the global economic crisis, there are factors that distinguish Deutsche Bank from the broader German co-determination example. In particular, there is the issue of the role of the bank workers' union at Deutsche Bank.[10]

Most German workers are covered under collective agreements that are negotiated for an entire sector, through sectoral mechanisms and employer associations.

10. More broadly, Germany's banks have a unique history and relationship to their national economy and German companies. German banks developed a close relationship with German companies after the Gründerkrise—a stock market crash – in 1873. Without developed stock and bond markets, German banks became major blockholders and creditors of German companies and were a provider of »patient capital«. This relationship existed for a century until 1993, when Germany had its longest recession since World War II. Germany modernized its financial system, expanded equity and money markets to increase global competitiveness, and implemented fundamental financial reforms in 2001 that gave a larger and more powerful role to shareholders. German banks' historical role as blockholders and creditors diminished as foreign investors, particularly hedge funds, began increasing their presence in Germany.

Figure 3. Level of Co-Determination and Income Equality



Source: Hans-Bockler-Stiftung. (2018). «Why Co-Determination? A collection of good arguments for strong workers' voice«.

This does not obligate German employees, however, to be members of the unions that negotiate these contracts. The OECD has estimated that 56 per cent of German workers were covered under collective agreements in 2016, but only 17 per cent were members of unions (OECD.Stat, Labour, 8 July 2018).

In its annual reports, Deutsche Bank has been estimating since 2012 that approximately 25 per cent or less of its estimated 100,000 employees are members of unions, including the public Postbank, in which 60 per cent of employees are members of unions. In Germany, where almost half of Deutsche Bank's workforce resides, in total in 2016, 17 per cent of employees were members of trade unions, while 56 per cent were covered under collective agreements in 2016.

What's more, over 40 per cent of Deutsche Bank global employees work in the private and business clients segment at present. An informative 2005 case study of the Deutsche Bank EWC noted that about 40 per cent of Deutsche Bank's workers were employed by then-recently acquired investment bank Morgan Grenfell, which had no employee representation (Eurofound, 2005). Therefore, it is likely weak member organization in Germany and a lack of union representation more broadly have created a weak union and EWC at Deutsche Bank.

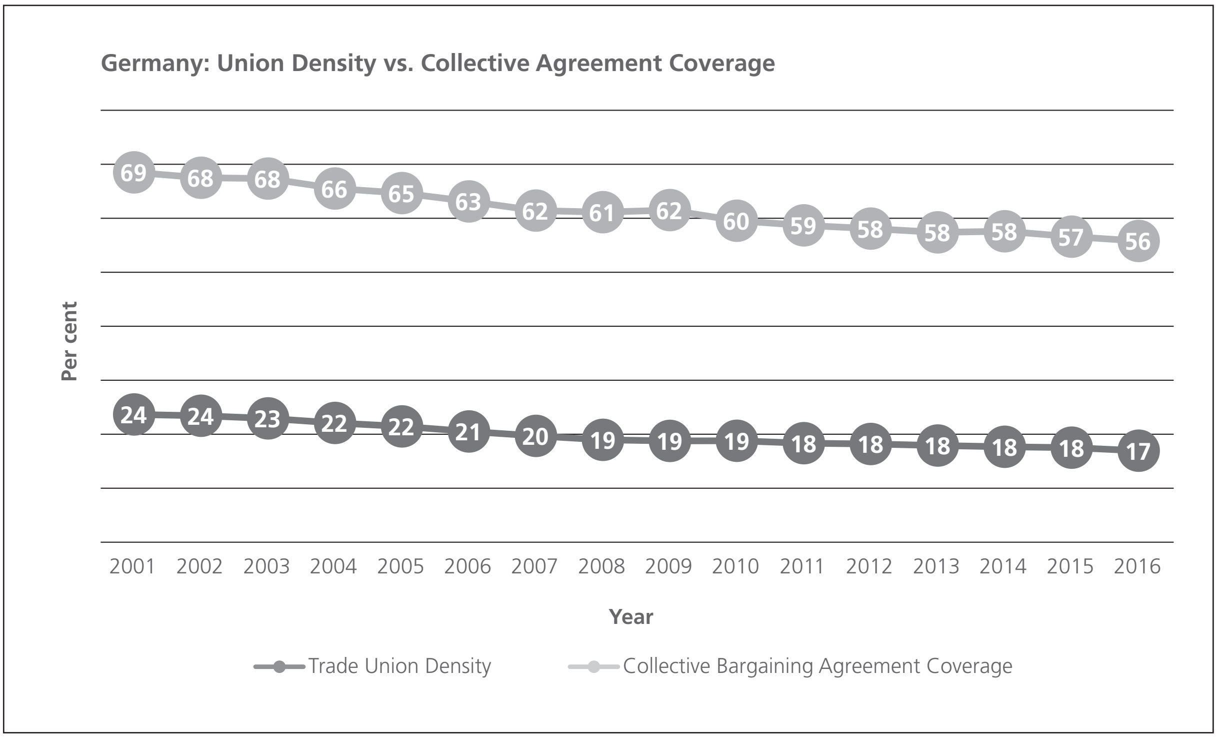
Thus, the Deutsche Bank example is an outlier in a broader co-determination structure that in general is fairly well integrated into Germany's system of labor-management relations. More generally, however, the co-determination model of including worker voice in corporate governance offers an invaluable template for effective »regulation from below.«

Argentina and Financial Instability

Quality employment[11] plays a key role in economic growth and the macroeconomic stability of any country. The consequences of instability are well documented—from decreased income and savings, and lower productivity, to reduced foreign investment. This is particularly observable in the context of severe financial instability.

11. Quality employment refers to stable employment in the formal economy, among other things.

Figure 4. Trade Union Strength in Germany



Source: OECD.Stat, Labour, »Trade Unions and Collective Bargaining: Collective bargaining coverage and trade union density in OECD countries«, 8 July 2018.

Strong policies that strengthen labor market institutions, however, can protect against some of these negative impacts by creating and protecting stable and high-quality formal jobs (Bertranou and Casanova, 2016).

The Argentinian example is instructive on this point. In the last 50 years, the country has undergone successive economic failures. Through much of that history, policy makers associated with the IMF and other multilateral institutions have often considered strong unions and labor protections to be part of the problem, and there were attacks on workers' rights and workers' voice in Argentina in the 1990s in response to those pressures. More recently, however, the country's labor institutions and policies have strengthened considerably, producing a visible correlation with improved macroeconomic stability (Bertranou and Casanova, 2016).

Argentina faced two major financial crises: hyperinflation in the early 1990s and the 2001 currency crisis. The chart below identifies the shift in both macroeconomic context and the prevailing attitude toward organized labor before and after 2001. In the 2000s, with a great need to increase quality *formal* employment (as opposed to informal work, which does not yield tax revenues), the country revitalized »institutions involved in setting wages and the administration of labor« and strengthened labor laws and policies in areas including job training and educational support, health care benefits, social security support, payroll subsidies, and child care (Bertranou and Casanova, 2016).

This example offers important insight into the role that a strong labor sector can play in supporting the macroeconomic health of a country. When the global financial crisis of 2008–2009 came, Argentina withstood the shock far better than it had during either of its previous crises. It sustained a positive GDP throughout the following years—a stark contrast to 1995, 1999, 2000, 2001, and 2002, when GDP dropped deeply into negative numbers (Bertranou and Casanova, 2016). Giving workers a voice through their unions also probably helped the country support more sound financial policy than it had in the past, making the country more stable and resilient in the face of internal and external economic shocks.

Figure 5. Employment Policy: Two Contrasting Periods Before and After Argentina's 2001 Crisis

The 1990s	The 2000s
Predominance of the Washington Consensus in the development of public policy	High real exchange rate
Structural adjustment	Increased competitiveness
Fixed exchange rate—convertibility with the peso pegged to the dollar, growing debt	Growth with high level of job creation
Privatizations	Increase in formal employment
Deregulation	Central role of labor institutions: collective bargaining, minimum wage, workplace inspection
Growth with low levels of job creation	Development of a network of public employment unions
Flexibilization of the labor market	Drop in inequality
Compensatory labor market policies	Substantial increase in tax to GDP ratio
Increase in informal employment and inequality	

Source: Bertranou, Casanova, Jimenez and Jimenez (2013).

Conclusion

Engaging workers through collective bargaining in the governance of financial institutions can have multiple benefits for risk mitigation at both firm and macroeconomic levels. An engaged and organized workforce is able to provide »regulation from below« that can meaningfully supplement and strengthen risk management by firm managers and regulators alike.

Unionized bank workers are more able to identify risks early, elevate them to senior leadership, and communicate vertically and horizontally throughout, between, and beyond institutions. Where workers' voices have been meaningfully incorporated into the governance structure, they appear to have provided an effective check on some of the worst tendencies of management (e.g., excessive executive compensation, prioritizing shareholder returns over necessary reinvestment). Additionally, there are clear correlations between strong unions with a role in governance and the broader stability of both the workforce and firms, particularly in a crisis; strong unions are also negatively correlated with income inequality, both within firms and within the labor market as a whole.

Nonetheless, the United States remains particularly hostile toward workers' rights, a hostility that has left bank workers in the country without a meaningful voice. This has negative implications for the stability of the U.S. banking system, and in light of the size of the U.S. banking system, for the global financial system. U.S. banks and U.S. subsidiaries of foreign banks have opposed workers' efforts to unionize, even at institutions that have positive labor relations with unions in other countries. Even as the risks created by financialization continue to grow (e.g., deregulation, income inequality, etc.), U.S. banks allow no meaningful role for workers in their governance processes.

Given the complexity of financial institutions and the persistent difficulties in overseeing and managing risk in the sector, policy makers should consider the potential of empowering worker voice to form »regulation from below.« There are several specific ways to support this objective that can be implemented by firm managers and directors, policy makers at all levels, and multilateral institutions, among others. Some of those ways include:

- *Adopting a policy preference for workers to be organized in unions.* Employers in the financial sector benefit from consultation and communication with employees regarding firm operations, without the many filters of middle management. Strong unions enable the workforce to formulate and express views independently of management. Additional research is required to identify structures that best ensure the independence of the unions from management to maximize the chances of successful »regulation from below.«

■ *Ensure workers can exercise their rights to be organized in unions and collectively bargain.* At a minimum, financial firms with significant global operations should operate within the framework of the ILO's core labor standards. In the U.S., existing labor law does little to protect employees' fundamental human rights and allows employers to undermine collective action, to the point that it has become a science. In light of the shortcomings of worker protections under U.S. law and the pervasive hostility toward worker organization in U.S. business culture, global firms should take a more proactive approach to encouraging worker voice. For example, financial firms operating in the U.S. could adopt a position of »neutrality« toward worker organizing. Governmental actors can support policies that facilitate workers' freedom of expression, organization, and collective bargaining, rather than undermine it with policies such as the deceptively named »right to work« laws that undermine core labor standards.[12]

■ *Including worker voices in governance solutions.* Formally providing a voice for workers in the governance of an institution has been shown to provide multiple benefits that accrue not just to workers, but also to shareholders, the firm, and the broader economy. Two effective existing models include the German co-determination model and the European Works Council model (especially effective in the »Nordic Model« in which there is a high level of union engagement).

■ *Supporting research into the positive role of quality jobs and strong labor institutions.* This paper has laid out several ways and instances in which the presence of strong labor institutions have supported better outcomes for multiple stakeholders, yet research in this policy space remains scant. The neoliberal brand of capitalism has grown from a theory of finance to an ideology, even as the empirical basis for many of its fundamental assumptions has been eroded. There is growing evidence, on the other hand, that good jobs and strong labor institutions can support macroeconomic growth and stability (e.g., by supporting aggregate demand and stabilizing the workforce in a crisis). Additional research and reporting are needed to understand these dynamics, identify optimal structures, and ultimately facilitate a shift toward new thinking about risk management in the financial sector.

■ *Multilateral Institutions incorporate and/or condition loans on the model of »regulation from below.«* Multilateral Institutions (MIs)[13] play a key role in managing international financial stability and thus should have a special interest in supporting »regulation from below.« MIs are also often well positioned to do so and frequently make policy recommendations on financial regulations and labor market policies at the national level. In such recommendations, MIs can help incorporate the model of »regulation from below.« The role of worker voice in the governance of financial institutions should be included in the total mix of information in MIs' decision making. Finally, MIs should, at a minimum, be engaged in routine dialogue with workers, their unions, and other representative bodies.

■ *Multilateral Institutions should support policies that lower economic inequality and instability.* In places where labor market institutions have functioning national- or sector-level collective bargaining that benefit workers, especially during times of economic instability or crisis, MIs can support the continuity of these policies. These actions align with MIs' mission of promoting financial stability, inclusive growth, as well as lower inequality and its accompanying risks.

The United States plays a dominant role in the global financial system. At the same time, U.S. financial firms have repeatedly experienced failure in risk management and oversight, whether in specific instances like the Wells Fargo accounts scandal, or more broadly in the case of the Great Recession of 2008. The potential for strong unions and worker voice to mitigate risk in the corporate structure and in the broader economy has been demonstrated in various contexts and models around the world. Thus it would be to the benefit of all stakeholders—firm management and directors, governmental overseers, shareholders, workers, and the broader economy—for U.S. financial firms to build positive labor relations with an organized workforce.

12. The misleading »right to work« label refers to state laws that prohibit employers and unions from agreeing that all represented workers shall pay union dues if they are members, or pay agency fees to the union if they are not members. Under U.S. law, no worker can ever be compelled to become a union member. The Supreme Court has just decided that, in public-sector employment, compulsory payment of agency fees by non-members who object to such fees is unconstitutional. The decision does not affect private-sector workers and unions.

13. Multilateral Institutions include Group of 20, Group of 7, the International Labour Organization (ILO), the Organization for Economic Co-operation and Development (OECD), the World Bank, International Monetary Fund (IMF), and Financial Stability Board (FSB), among others.

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Acknowledgments

The authors would like to thank Shannon Bade, Cecilia Begham, Teresa Casertano, Lance Compa, Heather Slavkin Corzo, Angelo DiCristo, Erin Mahoney, Dan Mauer, Patrick O'Meara, Arnise Porter, Brandon Rees, Sandy Rusher, Grace Sheedy, and Damon Silvers.

Imprint

Friedrich-Ebert-Stiftung | Global Policy and Development
Hiroshimastr. 28 | 10785 Berlin | Germany

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ISBN
978-3-96250-041-2