

# ***The Banks and Society: Rebuilding Trust***

## ***Social, ethical and environmental concerns***

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### **EXECUTIVE SUMMARY**

The 2007-10 banking crisis and recession have badly eroded trust in the banks. Besides the question of financial system stability, banks have been increasingly criticised for contributing to environmental, social and human rights problems. An adequate response to all these issues is required if banks are to regain public trust.

This report discusses social, ethical and environmental concerns arising from banks' direct impact on customers, employees, and local and national communities; from indirect consequences that can occur as a result of banks' facilitation of clients' business; and from banks' corporate governance.

The report also provides a summary of the activities that banks undertake and brief profiles of the main banks operating in the UK and Ireland. It includes questions to help stakeholders engage with banks over issues of concern, recommendations to improve banks' corporate responsibility performance, and sources of further information.

### **Issues raised**

Among the main issues raised in the report are that:

- Most banks' business model excludes some individuals and businesses from accessing financial services, especially in disadvantaged areas.
- Bank lobbying has had considerable impact on public policy and is far from transparent.
- Despite voluntary codes and statements about incorporating social and ethical concerns into lending decisions, banks still lend to environmentally and socially destructive projects.
- Banks' services may have facilitated illicit flows of money from developing countries.
- Banks have been associated with non-payment of tax due and non-compliance with the spirit of taxation law.
- Banks continue to have a role in the debt crisis faced by developing countries.
- Investment banks' speculative trading appears to have exacerbated recent food and fuel price spikes.
- Banks' and regulators' collective failure of judgement was a major cause of the financial crisis.

Based on the report's findings, and on its recommendations directed at what the banks should do to rebuild public trust, a picture emerges of what a more socially and environmentally responsible banking sector would look like. While better regulation is needed, much can be achieved by the banks' taking corporate responsibility more seriously.

Many banks now recognise some responsibility in these areas. But - beyond those few financial institutions that have developed with ethical principles at their core - most do not yet effectively integrate social and environmental issues into their core business activities.

The need for greater transparency is clear. On many issues there is often insufficient information for outsiders to make informed judgements about banks' performance.

## **Recommendations**

The report makes recommendations on thirteen social, ethical and environmental concerns material to most of the major UK and Irish banks.

### ***On customer service, banks should:***

- Work to achieve consistently positive customer feedback.
- Reduce the proportion of customer complaints upheld by the banking ombudsman.
- Strengthen the way they monitor and rectify complaints.
- Be more transparent about the interest rates they offer and charge.

### ***On financial exclusion, banks should:***

- Publish information, and ensure staff follow government guidelines, on alternative identification allowed for new customers.
- Publicly report the number and percentage of active basic bank accounts they hold and about lending to small businesses in deprived areas.
- Be more transparent about penalty charges.
- Train and encourage frontline staff to recommend basic bank accounts.
- Work harder to maintain counter services when they are the last financial institution in a community.
- Consider changes to account facilities for marginally financially excluded customers.
- Do more to support, and when appropriate refer customers to, community financial institutions.

### ***On responsible credit, banks should:***

- Publicly report the volume of credit they provide to individuals and businesses, broken down by demographic group and geographical area.
- Provide clearly written and non-misleading customer information on loans and other products.
- Have clear policies and procedures for fair and respectful treatment of individuals experiencing difficulty servicing loans, keeping home repossessions as an absolute last resort.
- Publicly report complaints or prosecutions upheld against them for unfair lending.
- Use remuneration structures for frontline staff to incentivise responsible lending.

### ***On gender equity in employment, banks should:***

- Work towards gender parity at all levels of employment.
- Publicly report on the gender balance of employees and at board level.
- Hold regular equal pay audits and publicly report top-level findings.

***On lobbying, banks should:***

- Fully complete the European Commission lobbying register.
- Publicly report on all other lobbying and representation likely to influence government policies.

***On lending, financing and asset management, banks should:***

- Have policies that preclude provision of services to socially and environmentally harmful projects and companies.
- Have policies to ensure that asset managers take full account of social and environmental considerations.
- Publish their social, ethical and environmental policies as applied to lending, financing, asset management and other services.
- Increase the proportion of their portfolio holdings in renewable energy, energy conservation and environmental protection projects.
- Include social and environmental analysis as a standard component of mergers and acquisitions advice and brokerage reports.
- Provide information about the companies and projects they fund and the social or environmental grounds on which they decline loans.
- Give deposit customers options to direct how their money is used.

***On money laundering, banks should:***

- Confirm the identity of all customers before accepting funds and have systems to identify Politically Exposed Persons (PEPs) and beneficial owners of companies.
- Refuse to open accounts for PEPs where precluded by the law of a PEP's country.
- Conduct enhanced due diligence on PEPs and sectors, companies and countries most associated with corruption.
- Publicly report prosecutions or fines for the contravention of anti-money-laundering regulations.
- Ensure their compliance department has an independent reporting line to the board.
- Create mechanisms to reward compliance officers even when their work leads to business being turned down.

***On tax avoidance, banks should:***

- Report on a country-by-country basis on all taxes they pay on their profits.
- Ensure that customers are aware of their own tax obligations.
- Refuse to provide tax planning that does not serve genuine business transactions.

***On developing country debt, banks should:***

- Publicly report on their exposure to developing country government debt.
- Carry out enhanced due diligence before committing to loans to developing country governments to avoid undermining poverty reduction.
- Apply social and environmental criteria to lending benefiting from export credit agency support.
- Publish non-confidential information about export credit agency arrangements.

***On commodity speculation, banks should:***

- Examine the social and environmental consequences of their speculative trading.
- Put limits on speculation where there is a risk of significant environmental or social harm.
- Trade derivatives transparently on regulated exchanges.

***On risk management, banks should:***

- Ensure senior level discussion of risk beyond use of standard risk management techniques.
- Continually evaluate their exposure to financial system risk and the extent to which they contribute to such risk.
- Apply the precautionary principle to minimise their contribution to systemic risk.
- Ensure a responsible attitude to risk throughout the business.
- Have an independent risk committee and publish an annual report of its activities.
- Ensure a balance between financial expertise and other experience among board members, particularly non-executives.

***On remuneration, banks should:***

- Take into account the views of external stakeholders when establishing remuneration policies and structures.
- Ensure that remuneration structures encourage responsible lending and discourage excessive risk taking; are commensurate with long term performance and shareholder value; include consideration of social, ethical and environmental factors and indicators of customer service and fair resolution of complaints.
- Publish the absolute value of, and ratio between, the remuneration of their highest paid employee and the average salary of the lowest paid 10% of employees and seek to continually reduce this ratio.

***On transparency, banks should:***

- Produce a separate, externally verified corporate responsibility report that at a minimum follows Global Reporting Initiative guidelines.
- Publish all policies on social, ethical and environmental issues.
- Be transparent about how they are likely to use depositors' money, giving examples of the activities and businesses they finance.
- Provide stakeholders with meaningful information on the issues covered in this report, including the indirect impact of their lending.

**Using the report**

The report is intended primarily for shareholders in, and customers of, banks in the UK and Ireland and for those advocating and working for a more socially responsible financial sector. It aims to help stakeholders analyse the impacts of banks they may own shares in, or bank with, and the extent to which any particular bank has a good record on a particular issue. We hope that the report will help people and organisations identify a bank whose policies and practices are relatively well aligned with their values.

ECCR also offers the report to bank boards and directors as they seek to improve their corporate responsibility performance, and to regulators and public policy-makers as they consider the sector's future.

**Questions to ask banks*****Questions to ask banks about customer service***

- What do the bank's own surveys show about levels of customer satisfaction, and how does this compare with surveys carried out by market research companies and consumer groups?
- What percentage of customer complaints does the bank resolve within eight weeks?

- What processes has the bank put in place to improve its customer service and complaints handling?
- What proportion of complaints referred to the ombudsman service has been upheld in favour of the consumer over the last 18 months? Is this higher or lower than average for the sector?

***Questions to ask banks about financial exclusion***

- Is it bank policy to accept all documents permitted by government guidelines as proof of identification for opening an account? If there are exceptions, what are the reasons for this?
- How does the bank ensure that all branch staff and potential customers are aware of its identification policy?
- How many active basic bank accounts does the bank service? How many of these were opened in the last 12 months?
- What proportion of frontline branch staff are knowledgeable about and can promote basic bank accounts?
- What is the bank's policy on closing the 'last bank in town'?
- How does the bank ensure that remuneration structures of frontline staff reinforce the need to provide good customer service?
- How does the bank ensure its products genuinely meet the needs of customers who are at risk of financial exclusion?
- What is the bank doing to promote financial capability?
- How does the bank support community financial institutions as part of 'community investment' or other programmes?

***Questions to ask banks about credit***

- What are the proportion and value of the bank's impaired loans (loans unlikely to be collected in full) compared to its competitors?
- Has the bank sought to improve its credit vetting process, and if so how?
- Does the bank publish statistics for lending by demographic group and geographical area? Does it encourage other banks to do the same?
- How does the bank address the issue of access to affordable credit?
- Has the bank been the subject of advertising or marketing complaints with respect to credit facilities? Have any such complaints been upheld?
- Has the bank been the subject of unfair lending complaints upheld by regulatory bodies?
- What is the bank's approach to customers experiencing difficulty in servicing loans?
- How many homes has the bank repossessed in the last year? What proportion of the bank's mortgages does this represent, and how does this compare to competitors' repossessions?
- How does the bank ensure that remuneration structures for staff involved in selling loans or other products support responsible lending practices?

***Questions to ask banks about gender equity in employment***

- What proportion of the bank's employees are women at board, senior and mid-management level? Does the company consider this sufficient?
- Does the bank have targets for female representation at board and senior management level?
- Does the bank operate a flexible working policy, and if so how far is this taken up within different divisions and levels of staff seniority?
- Does the bank undertake equal pay audits? If so, are the headline findings and resulting action plans published?

- Has the company had complaints of gender discrimination upheld at employment tribunals?
- Are employees subject to gagging clauses preventing them from comparing pay and bonuses for similar jobs?

#### ***Questions to ask banks about lobbying***

- On what major issues has the bank sought to influence government or intergovernmental bodies? What specific changes have been sought?
- Does the bank use the services of lobbying or public affairs companies? If so, which?
- On which, if any, official committees or expert groups is the bank represented? Is this disclosed in the company's annual report?
- What industry associations does the bank belong to?
- How much money has the bank spent on lobbying over the last three years?
- Is the above information published by the company and available to stakeholders? If not, why not?

#### ***Questions to ask banks about lending, financing services and asset management***

- If the bank is involved in asset management, has it signed up to the UN Principles for Responsible Investment? If not, why not?
- If the bank is involved in project lending or advisory services, has it signed up to the Equator Principles? If not, why not?
- Which social, ethical and environmental issues does the bank take into account when deciding to provide financing or asset management? Do the policies have clear limits, specifying activities that the bank considers inappropriate to be associated with?
- Does the bank make policy documents on these issues publicly available?
- What proportion of the bank's lending portfolio supports renewable energy, energy conservation and other environmental protection projects?
- If the bank provides brokerage reports or mergers and acquisitions advice, is social and environmental analysis routinely included?
- Does the bank report on its lending activities in a way that enables stakeholders to understand how effectively it implements its ethical policies?
- Does the bank offer asset management customers 'ethical', 'socially responsible' or 'sustainable' investment options?
- Does the bank offer deposit customers a choice about the type of activity their money can be used for?

#### ***Questions to ask banks about money laundering***

- Has the bank been prosecuted or fined for contravening anti-money-laundering laws?
- What systems does the bank have to identify Politically Exposed Persons (PEPs) and their source of funds?
- Does the bank identify sectors and countries that require enhanced due diligence?
- What are the bank's policies with respect to doing business with PEPs? Does it refuse to operate accounts for PEPs where that would be prohibited by laws in their country of origin or to accept funds where there is not strong evidence that these are legitimate? What enhanced due diligence systems exist?
- Does the bank's compliance department have an independent reporting line to its board?
- How does the bank reward compliance officers, given that effective work on their part may lead to business being turned down?

### ***Questions to ask banks about tax avoidance***

- Has the bank been successfully prosecuted for evading tax or been subject to public criticisms for tax avoidance?
- Does the bank operate branches or accounts in tax havens?
- Does the bank report on the taxation it pays on its own profits on a country-by-country basis?
- Does the bank provide tax planning services for clients? If so, how does it ensure that these do not have the effect of unfairly avoiding tax?
- Does the bank provide financial services to companies that have been successfully prosecuted for tax evasion? If so, has the bank sought to ensure that such companies are now tax compliant?
- Does the bank have a policy of only doing business for companies that report on the tax they pay on a country-by-country basis?

### ***Questions to ask banks about developing country debt***

- To what extent is the bank directly exposed to the internal/domestic or external sovereign debt of developing countries, or to the debt of state-owned companies in such countries?
- Has the bank benefited from export credit agency guarantees or insurance with respect to developing countries? If so, what due diligence did the bank undertake? Has the bank called upon those guarantees?
- What processes does the bank have to ensure that any exposure to developing country debt or involvement in export credit guarantees or insurance does not undermine poverty reduction initiatives?

### ***Questions to ask banks about commodity speculation***

- What proportion of the bank's turnover and profit is derived from commodity speculation?
- Does the bank voluntarily place limits on the volume of commodity derivatives it holds in individual markets?
- Has the bank examined the potential social and environmental consequences of its speculative trading activities? If so, what were the findings?
- Does the bank apply any ethical codes with regard to speculative trading activities?
- Is the bank engaged in lobbying with regard to the regulation of derivative trading?

### ***Questions to ask banks about risk management***

- How does the board set the bank's appetite for risk?
- How leveraged is the bank's balance sheet? (To what extent does the bank use borrowed money to supplement its own capital?)
- What has the bank done to establish a culture of risk awareness and to integrate risk management into its business functions?
- In light of criticisms of standard risk management techniques, how will the bank analyse and manage risk beyond what is required by regulatory standards?
- How many times has the bank's risk committee met? Have the non-executive directors on the committee sought external advice on risk issues?
- What are the background and experience of the bank's non-executive directors?
- How does the bank identify the extent to which it is exposed to, and contributes to, systemic risk to the financial system?
- How does the bank minimise its contribution to systemic risk?

### **Questions to ask banks about remuneration**

- What is the ratio between remuneration of the highest paid member of staff and the average of the lowest paid 10%?
- When the bank makes a loss, does it pay any discretionary bonuses? If so, why?
- Does the bank publish its remuneration policy?
- Does the bank's remuneration policy look at non-financial measures? If so, which measures?
- Does application of the policy to branch staff and senior retail executives take into account levels of customer satisfaction and fair resolution of complaints?
- How does the remuneration policy ensure that employees work in the long term interests of the bank and its shareholders rather than for purely personal rewards?
- Does the bank's remuneration committee take into account the views of employees, customers, shareholders and the wider society when setting and implementing remuneration policy?

### **Questions to ask banks about transparency**

- Does the bank produce a separate corporate responsibility report or maintain a significant corporate responsibility section on its website?
- Does the corporate responsibility report follow Global Reporting Initiative guidelines?
- Is the information provided externally verified?
- On which of the issues covered by ECCR in this report does the bank provide information?
- Does the bank publish information on the social, ethical and environmental policies it applies when making decisions about lending or providing other financial services?
- Does the bank provide information about the companies and projects that it lends to?

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