Five years after the bankruptcy of Lehman Brothers, Wall Street has made an impressive comeback. The industry is adapting to regulatory reforms and other challenges, and has been profitable for four consecutive years (including the three best years on record). While the risk of another financial crisis has been reduced, the firms that were seen as “too big to fail” during the financial crisis are even larger today.

The broker/dealer operations of New York Stock Exchange member firms (the traditional measure of industry profitability) earned $23.9 billion in 2012, the third-highest level on record and higher than any year before the crisis. The industry was on pace for another good year, earning $10.1 billion in the first half of 2013, but higher interest rates, litigation costs, and the turmoil over the federal budget and the debt limit could hold down profitability in the second half.

Even though the securities industry has been profitable in recent years, the number of jobs in the industry in New York City has not returned to the level reached before the crisis. The Office of the State Comptroller (OSC) estimates that there are 13.5 percent fewer jobs in the industry than before the financial crisis. OSC expects that the securities industry will continue to reorganize and streamline as it adapts to regulatory changes.

Compensation practices have also changed since the financial crisis. Base salaries are higher, and a smaller share of bonuses is paid in cash while a larger share is deferred to future years. Although compensation trends during the first half of 2013 suggested bonuses might be higher in 2013, recent developments have cast doubt on that outlook.

The securities industry has undergone changes since the crisis, but it is still profitable, well-compensated, a major contributor to State and City tax revenues, and a driving force in the economy. It remains to be seen, however, how future regulatory changes and rising interest rates will impact the industry. In the meanwhile, New York City remains the financial center of the world.
Regulatory Reforms

Implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act, signed into law three years ago, is proceeding slowly. According to the monthly Dodd-Frank Progress Report produced by the law firm Davis Polk & Wardwell LLP, the law requires 398 rules. Thus far, only 40 percent of the required rules have been completed, slightly more than the one-third share that had been completed by October 2012.

Section 619 of Dodd-Frank, known as the Volcker Rule, is designed to reduce unnecessary risk by restricting banks from trading on their own accounts (i.e., proprietary trading) and from holding an ownership stake in a hedge fund or private equity fund. The rule was expected to be finalized by July 2012, but completion has been delayed until the end of 2013 as a result of the heavy volume of industry comments. It is anticipated to take effect two years later.

Even though the Volcker Rule has not been finalized, some banks have begun to change their business in anticipation of the rule becoming law. For example, Citibank recently indicated that it was selling several private equity and hedge funds it operated, in order to comply with the rule.

To make up for lost revenue, the industry has entered into new businesses and expanded old ones. For example, fee income from wealth management and other investment advice rose by 71 percent between 2009 and 2012, and by another 23 percent in the first half of 2013.

Dodd-Frank, the Federal Reserve and certain international agreements all require banks to increase their capital reserves over time. The Federal Reserve has been conducting stress tests to determine whether the largest banks have enough capital to withstand potential losses resulting from a severe national recession and a global economic slowdown. The results of the most recent stress test, which were released in March 2013, found that only one of the 18 banks examined failed to meet the required capital-to-asset ratio, compared to four banks in 2012.

Profits

Securities industry profitability, traditionally measured by the broker/dealer operations of New York Stock Exchange member firms, has improved since the financial crisis. After two successive years of record losses in 2007 and 2008 (driven by large trading losses and a falloff in other revenues), the industry has had four years of profitability, including the three years with the highest profits on record (see Figure 1).

The significant rebound in profits during 2009 and 2010 (to the two highest levels on record) primarily reflected the impact of federal government support programs, including a reduction in short-term interest rates by the Federal Reserve to nearly zero percent, which reduced the industry’s interest expenses by nearly 92 percent between 2007 and 2010.
Profitability was more volatile during 2011. After a strong first half of the year ($12.6 billion in profits), losses mounted during the second half ($4.9 billion) as a result of the growing European sovereign debt crisis and weaker international economic growth. For all of 2011, profits totaled $7.7 billion, the lowest level in nine years except during the crisis.

Industry profitability was strong throughout 2012, reaching $23.9 billion (three times higher than the year before, and the third-highest level on record). In the first half of 2013, profits remained strong at $10.1 billion (close to the pace during the first half of 2012).

Several risks, however, could hold down profitability in the second half of the year. These include higher interest rates and litigation costs. A number of firms have already reached large financial settlements stemming from litigation and additional settlements are expected. The turmoil in Washington over the federal budget and the debt limit could also impact profitability.

Although industry-wide data are not yet available for the third quarter, earnings reports for most of the large firms were generally weaker. As a result, OSC estimates that broker/dealer profits could be limited to $15 billion in 2013, still higher than the forecast in New York City’s four-year financial plan ($13.4 billion).

Over the longer term, interest rates are likely to rise as the Federal Reserve changes its monetary policies, which could dampen profitability. Future regulatory changes that restrict certain business activities and others that require higher capital reserves might also limit profits, but these changes are designed to reduce the likelihood of another financial crisis. While the European sovereign debt crisis has stabilized, it has not been resolved.

**Employment**

Even though the securities industry has returned to profitability, the number of jobs in the securities industry in New York City has not returned to its prerecession level (see Figure 2). OSC estimates that the number of jobs in the industry totaled 163,400 (seasonally adjusted) as of August 2013 (the latest available data), which is 25,600 (13.5 percent) fewer jobs than before the crisis.

Although the securities industry showed strong job growth between January 2010 and August 2011 (adding 9,600 jobs), since then the industry has resumed streamlining (losing 7,300 jobs). While jobs have been added in risk management and regulatory compliance, employment in other segments of the business has contracted. Consequently, the industry has added a net of only 2,300 jobs since the recovery began. OSC expects the City’s securities industry to continue to reorganize and streamline as it adapts to its changing regulatory and economic environment.
While securities industry job growth has been weak, overall the City’s private sector has grown rapidly during the recovery, adding 335,000 jobs, or more than twice as many jobs as were lost during the recession. The number of private sector jobs in New York City has reached a record 3.4 million in 2013. There has also been a trend, however, toward lower-paying and part-time jobs.

Job growth in the securities industry in New York City has been much weaker during the current economic recovery than during past recoveries. So far, the securities industry accounts for less than 1 percent of the private sector jobs added during the recovery. During the comparable periods after both the 1990-1992 and 2001-2003 recessions, Wall Street had accounted for about 11 percent of the private sector job gains.

New York City accounts for about 89 percent of securities industry employment in New York State, a share that has declined only slightly over the past two decades. The City’s share of national securities employment, however, slowly declined from about 30 percent in 1993 to about 20 percent after the terrorist attacks of September 11, 2001, and has remained near that level since. Nevertheless, the number of securities industry jobs in New York State remains much larger than in any other state. California had the second-highest number of securities jobs, but the number of jobs in New York is almost 2.5 times larger.

**Figure 3**

Wall Street Cash Bonus Pool

![Graph showing Wall Street Cash Bonus Pool from 1990 to 2012](Note: Cash bonuses for securities jobs located in New York City; excludes deferred components that have not yet been paid.
Sources: NYS Department of Labor; OSC analysis)

**Bonuses**

Like most businesses, financial firms report compensation (i.e., base salary, fringe benefits and bonuses, including deferred remuneration) on an accrual basis of accounting. As such, cash bonuses paid in January through March of one calendar year (for work performed during the prior calendar year) are reported in the prior year’s financial statements. For example, most of the resources that are being set aside for cash bonuses in 2013 will be paid out during the first quarter of 2014.

Previously, most bonuses reflected work done in a given year and were paid in cash. This tended to reward short-term profits at the expense of long-term performance. In response to new regulations and other compensation reforms designed to reduce excessive risk-taking, firms have raised base salaries, and now pay a smaller share of bonuses in the current year while a larger share is deferred to future years in the form of cash, stock options or other forms of compensation. Clawback provisions have also been implemented. In addition, a greater share of bonuses is now being paid outside the traditional bonus period, making it harder to distinguish bonuses from base salaries.

While these developments have made estimating the size of the cash bonus pool more difficult, they have also reduced volatility in industry tax payments to the State and City. Collections now reflect an average of bonus payments from several years, allowing strong years to offset weak years.
In February 2013, OSC estimated that the cash bonus pool for securities industry workers in New York City paid during the traditional bonus season grew by 8 percent to $20 billion (see Figure 3). The increase in the size of the cash bonus pool reflects a number of developments, including payments received for work done in 2012, when profits were strong, and the realization of bonuses deferred from prior years (including income accelerated into 2012 from future years to avoid the higher federal income tax rates that took effect in 2013).

Total compensation for the broker/dealer operations of member firms of the New York Stock Exchange increased by 5.5 percent during the first half of 2013, and an OSC examination of the financial statements of a sample of large and small firms (including firms that engage in a broader range of activities than traditional broker/dealer operations) also found that compensation was higher than last year. These trends suggested that bonuses might be higher in 2013, but recent developments have cast doubt on that outlook. Although it is too early to predict the size of the 2013 bonus pool, bonus awards traditionally vary by firm and by business activity.

Increased regulation has also led Wall Street firms to make other changes to their policies on compensation. For instance, an advisory vote on compensation for named executive officers (known as “say-on-pay”) has been instituted, giving shareholders a stronger voice. Also, the European Union has begun to institute stricter limits on compensation that may impact employees of the affected companies worldwide.

### Average Salaries

The average salary (including bonuses) paid to securities industry employees in New York City grew rapidly from 2003 through 2007, when it peaked at $401,500. The average salary fell sharply in 2009 as the financial crisis deepened, but much of the loss was regained in 2010. Since then, salaries have remained stable, averaging $360,700 in 2012 (see Figure 4). While the 2012 average salary was less than the 2007 peak, it was higher than in any year prior to 2007, and was by far the highest average among the City’s major industries.

The disparity between the average salary in the City’s securities industry and in the rest of the private sector remains wide, even though recently it has narrowed slightly. In 2012, the average salary in the securities industry was 5.2 times greater than the average in the rest of the private sector ($69,200). At its peak in 2007, the average was 6.2 times greater. Twenty-five years ago, the average salary in the industry was twice as high as in other industries.
The average salary in the City’s securities industry remained substantially higher than the industry’s average in the rest of New York State ($226,100) and in the rest of the nation ($165,400). This reflects a concentration of highly compensated positions, such as chief executives and investment bankers, on Wall Street. While the average salary in the City remained below the 2007 peak, industry salaries set a new record in the rest of the nation in 2012.

Wages

Total wages, which is a function of the number of jobs and the average salary of those jobs, is an important measure of the economic impact of the securities industry. As OSC has noted in past reports, the securities industry accounts for a disproportionate share of wages in New York City. In 2012, Wall Street accounted for 21.9 percent of all private sector wages in the City, even though it accounted for only 5.1 percent of all private sector jobs.8

The total amount of wages (including bonuses) paid to securities industry employees located in New York City declined by 2.4 percent in 2012 to $59.3 billion (see Figure 5), reflecting a small decline in employment and average salaries. While total securities industry wages remain below the peak in 2007 (primarily reflecting the effects of downsizing), over the past three years total wages have been higher than they were during the years leading up to the financial crisis.

Tax Revenues

The high level of compensation in the securities industry, firm profits and capital gains realizations generated by securities-related activities yield significant tax revenue for New York City and New York State. OSC estimates that City tax payments (specifically in the general corporation, unincorporated business and personal income taxes) that are attributable to the securities industry increased by nearly 27 percent to $3.8 billion in City fiscal year (CFY) 2013, the second-highest level on record.9

The large increase in tax payments reflects improved profitability on Wall Street in 2012, but most of the increase resulted from an acceleration of income into 2012 to avoid higher federal tax rates that took effect on January 1, 2013. As a result of this strong growth, the securities industry’s share of City tax revenues (excluding audits) rose to 8.5 percent in CFY 2013, the highest level since it peaked in CFY 2008 (see Figure 6).10

New York State depends on Wall Street even more than New York City because the State relies more heavily on personal and business income taxes. The State also receives tax payments from the many industry employees who commute into the City from the surrounding suburbs (including those outside of New York State), and from the larger statewide pool of capital gains realizations.
OSC estimates that securities industry-related personal income and corporate Article 9A tax payments to New York State rose to $10.3 billion in State fiscal year (SFY) 2012-2013 (see Figure 7). While this represents only a small increase from the prior year, it was the fourth-highest level on record (and 15 percent higher than the recessionary low in SFY 2010-2011).

As a result, revenue derived from the securities industry accounted for nearly 16 percent of all State tax revenue in SFY 2012-2013. This is slightly more than in the preceding year, but still significantly below the recent peaks of more than 20 percent reached in SFY 2007-2008 and SFY 2008-2009.

OSC expects securities industry-related tax collections to be much higher in the current fiscal year (SFY 2013-2014). This is a result of the timing of the State fiscal year, which has caused the recognition of much of the tax revenue generated by the acceleration of income into 2012 from future years (to avoid higher federal income tax rates) to be delayed to SFY 2013-2014.
Economic Multiplier

OSC estimates that each new job created (or lost) in the securities industry leads to the creation (or loss) of two additional jobs in other industries in the City.\textsuperscript{11} The size of the multiplier reflects the high income levels associated with the industry and its importance in the City’s economy. These additional (or fewer) jobs result from Wall Street firms engaging in additional (or fewer) business-to-business transactions (e.g., with professional services firms and other financial firms), and from Wall Street employees increasing (or decreasing) their household spending on such things as restaurants, stores, travel and personal services.

OSC also estimates that each Wall Street job created (or lost) results in one additional (or fewer) job elsewhere in New York State, primarily in the City’s suburbs. Many Wall Street employees are commuters, who live and spend in the suburbs, thereby supporting local businesses and generating jobs.

In recent years, the securities industry has not stimulated significant employment growth in other employment sectors because job growth in the securities industry has been weak. Nevertheless, the securities industry remains a critical part of the New York State and New York City economies. Based on the multipliers and the current level of securities industry employment, OSC estimates that 1 in 8 jobs in the City and 1 in 13 jobs in the State are either directly or indirectly associated with Wall Street.

\textsuperscript{1} Davis Polk & Wardwell LLP counts requirements more than once when multiple agencies work on a rule or study.

\textsuperscript{2} These firms also engage in a broader range of activities beyond broker/dealer operations, which are not fully captured by this measure.

\textsuperscript{3} Securities industry employment data for September 2013 has been delayed as a result of the shutdown of the federal government.

\textsuperscript{4} OSC estimates that the securities industry in New York City lost 27,900 jobs between November 2007 and January 2010, and that it had regained only 8.4 percent (2,300) of those jobs as of August 2013.

\textsuperscript{5} The securities industry in the rest of the State had a smaller employment decline (10.7 percent) than in the City, and it has recovered a greater share of its job losses (nearly one-third).

\textsuperscript{6} Clawback provisions allow a firm to reduce or reclaim a portion of an employee’s bonus if the products or services upon which the bonus were based shift from generating profits to creating losses, resulting in an adverse impact on the firm. Such provisions ensure that employees work to produce long-term benefits for their firms.

\textsuperscript{7} These figures include payments to employees in cities around the world, but they suggest that the cash bonus pool could be higher for employees located in the City.

\textsuperscript{8} The securities industry’s share of private sector wages exceeded 28 percent in 2007 at the start of the financial crisis. The strong gains in employment in the rest of the City’s private sector since then have driven citywide wage growth, resulting in the reduction of Wall Street’s share of wages.

\textsuperscript{9} Taxpayer behavior has changed in recent years, which has been reflected in new and revised information. As a result, OSC has updated its estimates of securities industry tax payments to New York City and New York State compared with those published in earlier reports.

\textsuperscript{10} These estimates exclude revenue from real property taxes, real estate transaction taxes and sales taxes.

\textsuperscript{11} The estimate is derived from the IMPLAN input/output model. As income levels in the industry remain substantially higher than in other industries, the estimate of the multipliers has not significantly changed since the financial crisis.