EXPLORATION OF THE WELLS FARGO BANK ACCOUNT FRAUD CASE

APRIL 9, 2024

UNIVERSITY OF WALES TRINITY SAINT DAVID

Executive Summary

In September 2016, Wells Fargo Bank, a prominent commercial bank renowned for its solid operational practices in the United States, was embroiled in a scandal involving the falsification of account information. This scandal arose due to various factors, including an assessment mechanism that excessively emphasized short-term performance, an irrational corporate governance structure, a challenging external development environment within the global banking industry, formalistic protection of financial consumer rights, and inadequate attention and supervision by regulatory authorities towards operational risks.

The Wells Fargo scandal had profound implications for various stakeholders. The bank's share price plummeted, leading to the resignation of its CEO, widespread layoffs, a significant loss of customers, and even a shakeup within the entire banking industry.

This episode serves as a stark reminder for financial risk prevention and control. Financial institutions must strive to improve their long-term compensation mechanisms and enhance sound corporate governance practices. Regulatory authorities, on the other hand, need to enhance the protection of financial consumer rights and strengthen the organic integration of systemic risk and individual institution risk supervision. By addressing these issues, the financial industry can move forward in a more stable and sustainable manner.

Keywords: Wells Fargo Bank, Operational risk, Corporate governance, Internal control system

Table of Contents

Executive Summary 1
Introduction 3
1 Basic Introduction of Wells Fargo Company 4
1.1 Wells Fargo's business situation 4
1.2 Buffett's "favourite stock" 5
1.3 Main business feature：Community banking 6
1.4 The primary marketing model： Cross-selling 6
2 The Wells Fargo account forgery case 7
2.1 A Review of the Wells Fargo Counterfeiting Process 7
2.2 Penalties Received by Wells Fargo 8
3. Analysing the reasons for Wells Fargo's forgery 8
3.1 Unreasonable performance appraisal mechanism 8
3.2 Inadequate corporate governance structure 8
3.3 A severe external environment of global banking industry 9
3.4 The protection of financial consumer rights and interests is a mere formality. 9
3.5 Insufficient attention to and regulation of business operational risk. 10
4 Implications of the Wells Fargo Account Fraud - Stakeholder Theory 10
4.1 Impacts on various stakeholders 10
4.2 Impact on the company's reputation and market value 12
5. Insights and recommendations 13
5.1 Recommendations for rich countries 13
Conclusion 14
Bibliography 16

Introduction

In recent years, the United States has witnessed numerous high-profile corporate fraud cases, including the Enron scandal in 2002, the Madoff fraud in 2008, and the Wells Fargo account falsification incident in 2016. This paper focuses on the Wells Fargo scandal, examining its underlying causes and exploring the issues pertaining to corporate governance and internal control within the bank. The aim is to draw lessons for enhancing financial market supervision and risk prevention.

Wells Fargo, founded in New York City in 1952, established itself as a reliable and well-managed institution. In 1998, it merged with Northwestern Bank, relocating its headquarters to San Francisco and retaining the Wells Fargo name. Notably, during the 2008 global financial crisis, when many major US banks struggled, Wells Fargo emerged as a resilient player, growing significantly. In 2015, it achieved a remarkable feat, surpassing the Industrial and Commercial Bank of China (ICBC) and JPMorgan Chase in terms of market capitalization, becoming the largest bank in the world.

However, this reputable institution's image was tarnished in September 2016, when it was exposed in a fraudulent account information scandal. This revelation shocked and outraged consumers and regulators alike. The question arises: what motivated Wells Fargo to falsify information and deceive its customers? Furthermore, what are the implications of this incident for various stakeholders? How can such fraud be prevented in the future? This article delves into these issues in the subsequent sections.

1 Basic Introduction of Wells Fargo Company

1.1 Wells Fargo's business situation

Wells Fargo Bank is a renowned international financial institution in the United States, offering a diverse range of financial products and services. As a crucial subsidiary of Wells Fargo & Company, it has earned a storied reputation over the years. Founded in San Francisco in 1852, Wells Fargo & Company has grown into a globally recognized enterprise after a century and a half. It has been ranked 25th on the list of the largest companies in the United States by the internationally renowned magazine Fortune. Notably, it is the only bank in the U.S. with an AAA credit rating.

In 2017, Wells Fargo reported assets worth 195billionandastaggeringnetincomeof22.18 billion, representing a significant 51.1% of Wells Fargo & Company's total net income. The bank's reach extends to every corner of the United States, with at least one-third of Americans having utilized its services. Its extensive workforce of 263,000 employees ensures that customers are well-served across the country.

What sets Wells Fargo apart is its unique business philosophy and approach. Prior to 2008, many large U.S. banks focused heavily on investment banking. However, during the financial crisis, banks like Citibank, due to their centralized structure, suffered severe internal financial and operational setbacks. In contrast, Wells Fargo Bank's focus on retail banking and a broader range of business services meant its revenue sources were more diversified, thus buffering it from the crisis's worst impacts. This strategic shift proved pivotal in Wells Fargo's ascendance, allowing it to overtake competitors and emerge as a leader in the U.S. banking industry.Following the subprime crisis, the U.S. banking landscape underwent significant restructuring. Wells Fargo capitalized on this opportunity, experiencing rapid growth and solidifying its position as a benchmark enterprise in the country. Its resilience and innovative approach have been instrumental in its sustained success and global recognition.

Wells Fargo's three primary businesses are Community Banking, Wholesale Banking, and Wealth and Investment Management.

Community Banking is the cornerstone of Wells Fargo's operations, with a focus on serving the local community. It involves establishing branches throughout the United States to cater to the financial needs of residents and small to medium-sized enterprises. Credit business is a significant aspect of this segment, and Wells Fargo holds the position as the largest bank in the country for providing loans to micro and small businesses. This business line holds immense value for Wells Fargo, as it generates the largest percentage of profits for the bank.

Wells Fargo's approach to Community Banking is strategic and innovative. The bank conducts extensive market research, segmenting the market to identify industries where lending can be most profitable. By standardizing its processes, Wells Fargo is able to achieve economies of scale, reducing costs and mitigating risks. Its vast network of over 9,000 branches across the U.S. offers a diverse range of financial services, exceeding 80 types, ensuring that customers' needs are met efficiently and conveniently.This extensive coverage not only enhances customer satisfaction but also reduces unnecessary expenses and facilitates the development of new business opportunities. Community Banking has been instrumental in Wells Fargo's growth, consistently generating significant profits. From 2015 to 2017, community banking revenues were 49.3billion,48.9 billion, and $48.7 billion, respectively, accounting for a substantial portion of Wells Fargo's total revenues. Similarly, net income from this segment remained robust, contributing significantly to the bank's overall profitability.

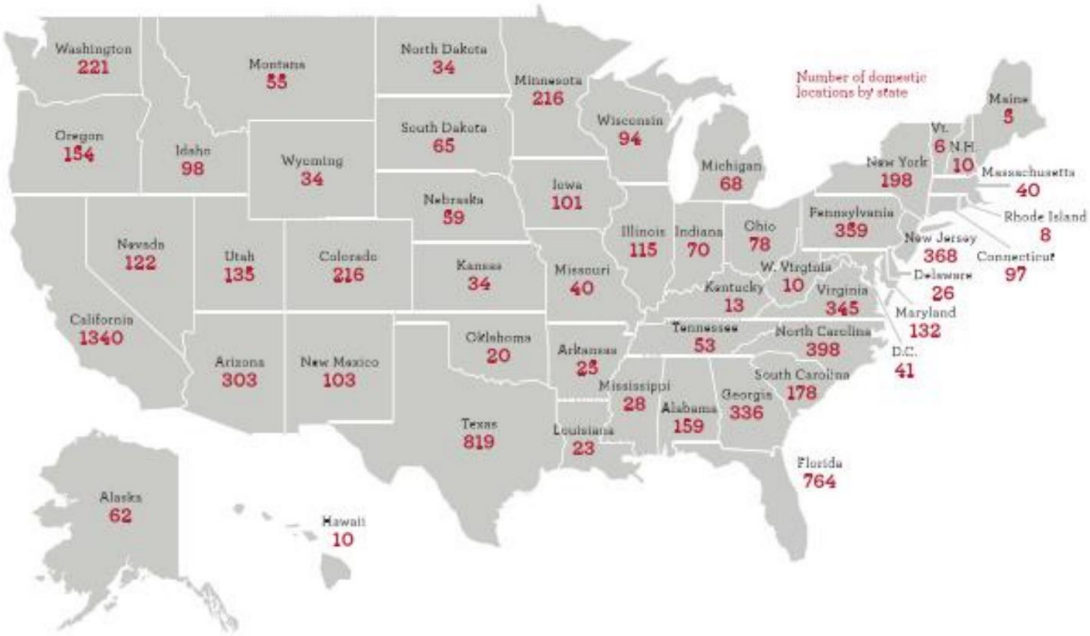

Figure 1-1 Distribution of Wells Fargo branches in the United States by state (home)

In addition to Community Banking, Wholesale Banking and Wealth and Investment Management are also crucial components of Wells Fargo's business model. Wholesale Banking caters to the financial needs of larger businesses and institutions, while Wealth and Investment Management focuses on providing personalized wealth management solutions to high-net-worth individuals and families. Together, these three businesses form the foundation of Wells Fargo's diverse and profitable financial services portfolio.Wholesale Banking focuses on providing investment banking services to mid-sized and large companies. Wells Fargo provides this business primarily to the oil and gas industry. Wells Fargo's share of this market is relatively small because other U.S. banks are too strong in investment banking. The investment banking business is also expanding quietly while keeping the community banking business. Wealth and investment management business focuses on providing comprehensive financial counselling and management services to clients, such as retirement business, real estate business and so on.

Table 1-1 Main business segments of Wells Fargo and their revenue contributions

hundreds of millions of dollars

Business type	Turnover			Net revenue		
	2017	2016	2015	2017	2016	2015
Community Banking	487	489	493	121	124	134
Wholesale Banking	282	285	259	87	82	82
Investment Management	169	159	158	27	24	23

Source: Wells Fargo Annual Report (2017)

1.2 Buffett's "favourite stock"

Warren Buffett's "favourite stock," Wells Fargo, has generated immense profits for him. In 1989, amidst a deeply depressed real estate market, Wells Fargo emerged as a key player due to its

extensive real estate mortgage loans, positioning it at the centre of the crisis. However, Buffett rationally analysed the situation and concluded that even amidst market turmoil, a well-managed business would remain resilient. Consequently, by 1990, he had acquired 5 million shares of Wells Fargo, representing 9.7% of its total share capital.His foresight proved correct. By 2000, the value of his Wells Fargo shares had soared to $3.07 billion, achieving a return on investment of 9.61 times and an impressive annual return of 25.4%. Nevertheless, this growth paled in comparison to the performance of Citibank and JPMorgan during the same period. From 1900 to 2000, Wells Fargo grew by 900%, whereas Citibank rose by 2,122% and JPMorgan by 1,163%.Although Wells Fargo did not rank first in the banking sector, Buffett believed in its potential for growth, surpassing other banks. He famously stated that if he could choose only one stock, it would be Wells Fargo. This belief was further validated during the 2008 economic crisis, as Wells Fargo's focus on retail business, coupled with its flexibility and diverse operational areas, shielded it from significant losses. Remarkably, Buffett has held Wells Fargo shares for 30 years, the longest tenure he has maintained for any bank stock, reflecting his deep-seated admiration for this particular investment.

1.3 Main business feature：Community banking

1.3 Main Business Feature: Community Banking

Community banking is Wells Fargo's primary business segment, contributing significantly to its overall profitability. This profitability stems primarily from the bank's ability to offer lower deposit rates and generate higher interest income. Wells Fargo's extensive network of over 9,000 branches across the United States, many situated in community neighbourhoods, provides convenient financial services to residents, a distinct advantage compared to other banks. Additionally, community residents typically possess less bargaining power, enabling Wells Fargo to offer lower deposit interest rates.

The focus of Wells Fargo's community banking lending is on small and micro-businesses. Initially, the bank's lending activities primarily targeted customers with annual sales revenues below 10million.However,WellsFargosoonrecognisedtheinefficienciesofthisapproach,includingthecomplexityoftheloanreviewprocess,highcosts,andprolongedwaitingtimes.Inresponse,thebankrefineditslendingtargetsandmethods,introducingthe"enterprisepass"initiative.Thisinitiativetargetsbusinesseswithannualincomesbelow2 million, offering loans with a maximum ceiling of $100,000 USD and generating higher interest income. This innovative model distinguished Wells Fargo from its competitors and enabled it to thrive against the backdrop of the financial crisis.

1.4 The primary marketing model： Cross-selling

With the enactment of the Financial Modernization Act of 1999, which dismantled the barriers between commercial banks and other financial institutions, Wells Fargo recognized an opportunity to significantly enhance its profits through cross-selling. Cross-selling is a marketing strategy that involves offering related products or services to fulfill multiple customer needs.

The first benefit of cross-selling is its ability to significantly increase customer loyalty. Research indicates that when customers hold more than four products from a company, the customer churn rate can drop to 1%. This increased stickiness not only retains existing customers but also reduces the costs associated with acquiring new ones.

Secondly, cross-selling can lead to substantial increases in corporate profits. Wells Fargo's analysis reveals that as the number of products a customer holds increases, so does the bank's average annual income. For instance, when customers hold 1-5 products, the bank's average annual income rises by 1.7 million U.S. dollars. This figure jumps to 2.4 million for customers holding 6-10 products

and soars to 5.3 million for those with 11-15 products. Remarkably, when customers hold more than 25 products, the bank's average annual income can increase by a staggering 52.55 million U.S. dollarsThis exponential growth in profits with each additional product held by customers underscores the importance of cross-selling for Wells Fargo. As a result, the bank aggressively pursued this business model, and by 2016, before the Wells Fargo scandal, its customers held an average of 6.29 Wells Fargo products each.Cross-selling not only diversified Wells Fargo's revenue streams but also enabled it to hedge against risks. This diversification proved crucial during the subprime mortgage crisis in 2008, allowing Wells Fargo to buck the trend and weather the storm better than many of its peers.

In summary, the Financial Modernization Act of 1999 presented Wells Fargo with an opportunity to revolutionize its business model through cross-selling. By leveraging this strategy, the bank was able to significantly enhance customer loyalty, increase profits, and diversify its revenue streams, ultimately positioning itself for success even in the face of economic challenges.

2 The Wells Fargo account forgery case

2.1 A Review of the Wells Fargo Counterfeiting Process

John Stumpf, the CEO of Wells Fargo, is best known for saying "Eight is great". The idea is that Wells Fargo cross-sells so that each customer has at least eight Wells Fargo products or services in their possession. It's true that cross-selling can lead to exponential growth in revenue for the bank and increase customer stickiness. But in Wells Fargo's specific implementation process, the target is set too harshly, it does not fully consider the actual situation within the bank.

Wells Fargo every day on the basis of the indicators of the staff assessment, if the staff did not meet the requirements, the light will be punished, the heavy will be dismissed. However, the indicator was set too high, and the daily customer traffic was not enough to meet this requirement, and the employees could not meet the indicator requirement through normal sales means. So the employees resorted to some abnormal means. The employees made use of their position to get hold of the information of the customers, so many of them opened deposit accounts or credit card accounts without the knowledge of the customers by using the customers' information without authorisation, so that they could meet the target requirement for the day. According to the survey, similar incidents have been occurring since 2001, and as of the time the scandal broke out, Wells Fargo had opened as many as 2 million fraudulent accounts.

On 8 September 2016, the US Office of the Comptroller of the Currency (OCC), as well as the US Consumer Financial Protection Bureau (CFPB), following an investigation, confirmed Wells Fargo's violation of opening accounts without customer authorisation and imposed penalties. Its violations are as follows:

1. Opening accounts and making transfers without consent. As a result of the investigation, Wells Fargo opened 1,530,000 deposit accounts and made unauthorised transfers of customer funds without the customers' knowledge, resulting in customers paying administrative fees because their originally opened accounts were underfunded or even overdrawn. Approximately 85,000 customers paid this fee, which totalled $2 million.

2. Consumers unknowingly opened credit card accounts. As a result of the investigation, Wells Fargo opened approximately 565,000 unauthorised credit card accounts without the knowledge of the customers, who were required to pay Wells Fargo an administration fee and other fees. Approximately 14,000 accounts generated $403,000 in administrative fees.

3. Activating credit cards without the customer's consent and having Wells Fargo employees set up PIN codes.

4. Creating false email addresses in order to hide the creation of accounts from customers. Wells Fargo employees created non-consumer email addresses without customers' knowledge or consent to allow them to create accounts without difficulty.

2.2 Penalties Received by Wells Fargo

On 8 September 2016, the U.S. Consumer Financial Protection Bureau (CFPB) imposed penalties of a $100 million fine on Wells Fargo under the Consumer Financial Protection Act, prohibiting Wells Fargo from engaging in activities that violated consumer rights. The specific violations were: Wells Fargo used its position to misappropriated customer information, opened deposit accounts as well as credit card accounts without the customers' consent, and made private transfers of customer funds, resulting in insufficient account balances and unnecessary fees paid by customers. On 8 September 2016, the US Office of the Comptroller of the Currency (OCC) decided to impose a fine of $35 million on Wells Fargo. The specific violations were that Wells Fargo's senior management did not have a sound internal control system, failed to detect employee violations in a timely manner, and failed to control the development of the situation. The laws and regulations referenced included, among others, the September 2007 edition of the Bank Supervision Procedures, the January 2010 edition of the Large Bank Supervision Handbook, and the August 1996 edition of Consumer Compliance Management. On 9 September 2016, the Los Angeles Bar decided to fine Wells Fargo $50 million under the California Unfair Competition Law. The specific violations were that Wells Fargo's junior employees opened unauthorised accounts and transferred customer funds.

3. Analysing the reasons for Wells Fargo's forgery

3.1 Unreasonable performance appraisal mechanism

As the Wells Fargo account information falsification scandal came to light, the immense pressure faced by the bank's employees also came to the forefront. Those who were terminated from their positions revealed that Wells Fargo's employee compensation was directly tied to sales performance, and the achievement of these performance indicators was exceedingly challenging. Consequently, numerous employees were coerced into resorting to forgery as a means to meet their sales quotas.According to the American Association of Certified Fraud Examiners (ACFE), an employee's decision to commit fraud often hinges on a delicate balance between pressure, opportunity, and rationalisation of their actions — collectively known as the "fraud triangle". It is estimated that in any given organisation, approximately 5%-10% of employees will never engage in fraudulent activities, another 5%-10% will do so regardless of job-related pressures or opportunities due to personal motivations, and the remaining employees fall within the "fraud triangle", where their behavioural norms are greatly influenced by external factors. When confronted with intense pressure and relatively low costs for violating the law, employees may act irrationally and even engage in fraudulent practices.In the case of Wells Fargo, the unreasonable performance appraisal mechanism created an environment where employees felt compelled to meet unrealistic sales targets through unethical means. This, combined with the pressure and opportunities present within the organisation, led many employees to rationalise their fraudulent actions and ultimately engage in the falsification of account information.

3.2 Inadequate corporate governance structure

Prior to the revelation of the scandal, John Stumpf held the dual roles of chairman and chief executive officer at Wells Fargo, resulting in a highly centralised decision-making process within the

bank. Compared to other major banks, Wells Fargo's board of directors had a relatively low proportion of independent directors, and many directors had served for extended periods, with over half having tenures exceeding 10 years. This flawed corporate governance structure led to a concentration of decision-making power in the hands of the management team led by John Stumpf. When the bank's operations deviated from its strategic direction, these issues could not be promptly rectified.Following the global financial crisis in 2008, the Dodd-Frank Act passed by the U.S. Congress included provisions regarding the recovery of compensation for senior executives. However, these provisions were challenging to enforce in practice. Prior to the Wells Fargo scandal being made public, only the CEO of JPMorgan Chase faced a pay cut due to the "London Whale" incident, and the pay recovery provision was not strictly implemented.

After the Wells Fargo scandal was exposed, the bank, facing external pressure rather than regulatory mandates, rescinded equity incentive bonuses totaling 41millionforJohnStumpfand19 million for Carrie Tolstedt, a retail executive. Nevertheless, Carrie Tolstedt still received $124 million in stock dividends and other bonuses. In such an environment where disciplinary measures are lax, bank executives are strongly incentivised to engage in high-risk and even illegal activities.

3.3 A severe external environment of global banking industry

Behind the Wells Fargo scandal, inadequate corporate governance and internal control were significant internal factors. However, another crucial external cause cannot be overlooked: the unprecedented pressure facing the global banking industry. In September 2016, McKinsey & Company released a report titled "Global Analysis of Major Banks," which highlighted that the global banking sector was experiencing a period of decline. It estimated that only 60% of banks would survive, earning the report the apt nickname of "Banking Industry Death Note."Despite Wells Fargo avoiding collapse, its profitability suffered due to quantitative easing measures. To maintain its competitiveness in retail banking, the bank intensified its sales efforts and cross-selling strategies to boost profits. This led to Wells Fargo's management setting increasingly aggressive business evaluation targets, placing undue pressure on grassroots account managers. Faced with unattainable targets, many bank employees resorted to unethical or even illegal practices.

Therefore, the Wells Fargo scandal was not just a matter of internal mismanagement but also a reflection of the broader challenges and pressures facing the global banking industry.

3.4 The protection of financial consumer rights and interests is a mere formality.

The protection of financial consumers in the United States has a long history. Starting in the 1960s, with the expansion of retail financial services, a consumer protection movement gradually emerged, leading to an increased awareness of financial consumers' rights. Following the global financial crisis in 2008, the Dodd-Frank Act was enacted, which mandated enhanced information disclosure by financial institutions. This refinement of disclosure requirements aimed to empower consumers with the necessary information to make informed decisions.Concurrently, the establishment of the Financial Consumer Protection Bureau (FCPB) in the U.S. signaled a dedicated focus on safeguarding consumers in the financial sector. However, the newly formed bureau faces resource constraints, and the two-tier financial regulatory system poses challenges in coordinating efforts among different regulatory bodies.

A key aspect of financial consumer protection is the customer complaint database, which holds crucial information. Unfortunately, this database contains a significant amount of inaccurate data, and there is also a substantial volume of content that cannot be included. When responding to customer complaints, the FCPB often fails to conduct thorough verifications and relies heavily on the institutions involved to handle the matters internally. This approach partially explains why the

revelation of Wells Fargo's falsified account information in 2011 was delayed for five years before it was addressed effectively.

To address these challenges, there is a need for increased funding and resources for the FCPB, as well as improved coordination among regulatory agencies. Additionally, enhancing the accuracy and inclusivity of the customer complaint database is crucial to ensure that consumer voices are heard and addressed promptly. By taking these measures, the U.S. can strengthen its financial consumer protection framework and mitigate the risks of future scandals like the Wells Fargo case.

3.5 Insufficient attention to and regulation of business operational risk.

Prior to 2008, the U.S. financial regulatory system operated under a fragmented, multi-headed approach. This meant that various aspects of a financial institution's operations were typically subject to overlapping supervision by multiple regulatory agencies. This arrangement often resulted in regulatory inefficiencies, including both redundant regulatory efforts and gaps in coverage.

In response to the global financial crisis that erupted in 2008, the Obama administration pressed Congress to pass the Dodd-Frank Act. This landmark legislation aimed to significantly reform the financial regulatory framework, with a focus on mitigating the destabilizing effects of financial institution failures on the broader financial industry and the economy. Additionally, the Act placed greater emphasis on enhancing consumer protection measures.One of the key provisions of the Dodd-Frank Act was the strengthening of systemic financial risk regulation. This emphasized the Federal Reserve's (Fed) primary role in overseeing systemic risks within the banking sector and established clear mechanisms for addressing such risks. However, this heavier focus on systemic risks may have led to a relative neglect of operational risks within the financial industry.

The Wells Fargo account information falsification incident stands as a stark example of this operational risk being overlooked. Despite the fraud being an obvious case of misconduct, the regulator failed to give it adequate attention or respond promptly to consumer complaints. If not for the coincidence of the U.S. presidential election, Wells Fargo might have escaped with merely compensating its customers for their losses, avoiding any further penalties, and its CEO might have retained his position.This regulatory negligence, coupled with the fact that Wells Fargo had escaped serious punishment for operational violations during the financial crisis, likely contributed to a culture within the bank where operational risks were underappreciated and the falsification of account information was tolerated. This underscores the need for a balanced approach in financial regulation, one that addresses both systemic and operational risks equally and ensures that consumer protection remains a paramount concern.

4 Implications of the Wells Fargo Account Fraud - Stakeholder Theory

4.1 Impacts on various stakeholders

(1) Shareholders

On 8 September 2016, i.e. after the three agencies demanded Wells Fargo to pay the fine, Wells Fargo's share price plummeted and by the end of September 2016, Wells Fargo's share price had dropped by more than 10%. JPMorgan Chase also overtook Wells Fargo as the world's largest bank by market capitalisation as a result of the incident. Before that, Wells Fargo had been the world's largest bank by market capitalisation since 2013. Warren Buffett, who is Wells Fargo's largest shareholder, was also badly affected by it. Buffett's investment holding company, Berkshire Hathaway, also suffered a sharp drop in its share price of more than 2 per cent as a result of the incident. At the same time, Wells Fargo's business activities were also severely affected, and the

company needed to keep enough cash flow within the company to maintain the turnover, thus the dividend plan was also changed.

Figure 3-1 Sharp fall in share price

(2) Managers

In October 2016 Wells Fargo's Board of Directors decided that John Stumpf, Wells Fargo's Chairman and Chief Executive Officer, would leave the company with immediate effect, and that Stumpf would resign as a member of the Federal Reserve's Federal Advisory Council. Stumpf will not receive a severance package and forfeits $41 million in stock awards previously granted to him. Carrie Tolstedt, Wells Fargo's Executive Vice Chairman, retired early and was not eligible for severance pay and forfeited $19 million in stock awards previously granted to her, but received current compensation of $124 million, and neither Stumpf nor Tolstedt were eligible for 2016 bonuses.

(3) Employees

In the wake of the Wells Fargo incident, all of the basic employees implicated in the scandal have been dismissed, approximately 5,300 or 2% of the total workforce. About 10 per cent of those dismissed were in senior management. Meanwhile, the US Department of Labour is investigating whether Wells Fargo's direct dismissal of employees was justified.

(4) Customers

Wells Fargo was required to compensate its customers for the losses they incurred as a result of the opening of accounts by employees of the bank, and Wells Fargo compensated them in full, with an amount of $2.6 million. At the same time, the scandal caused a large number of customers to be lost, and Wells Fargo lost many important customers. For example, the California state government terminated its cooperation with Wells Fargo after the scandal came to light, the Illinois state government and the Seattle city government also announced that they would stop their ongoing business cooperation with Wells Fargo, and many private banking customers transferred their business to other banks.

(5) The entire banking industry

The continuing fermentation of the Wells Fargo scandal has plunged the U.S. banking industry into a new round of crisis of confidence. First, a series of other lawsuits against Wells Fargo have emerged and require further investigation. Most of these lawsuits come from Wells Fargo customers as well as employees who left Wells Fargo. These include, Wells Fargo forcing employees to buy stock when it was overvalued and even encouraging them to use their pensions to do so; Wells Fargo forcing employees to work overtime without reason; and firing employees for no reason when they failed to meet the sales targets set by Wells Fargo, among others. On top of that, Wells Fargo's subsidiaries are under investigation by regulators. Secondly, the Wells Fargo scandal led to other large banks being forced to undergo investigations. Morgan Stanley was also charged by the Secretary of the Commonwealth of Massachusetts for unethical cross-selling practices. Thirdly, the public questioned the banks' marketing methods. After the Wells Fargo scandal came to light, people were sceptical of cross-selling as a marketing method, believing that it did not bring convenience and meet their needs, but instead, they would be exploited for this reason by having their personal privacy and opening accounts without their knowledge.

(6) Government and Regulators

Wells Fargo used to serve as a model student of the US banking industry, and this account forgery case has caused the public to question the financial regulatory system, and at the same time, it will also promote the reform of the US financial regulation, such as improving the system of correlating the bank's performance with the executive's compensation, as well as the system of recovery of executive compensation, which has been seldom enforced in the past. Previously, the Dodd-Frank Act in the United States of America's executive compensation recovery system is seldom implemented, and this time, leaving the executive compensation recovery, not in violation of the U.S. Securities and Exchange Commission (SEC) law, but based on external public opinion pressure and internal decision-making of the bank after the results of deliberation. In the future, regulators will enforce the rules more strictly, pay more attention to the duties of bank executives, and speed up the implementation of laws and regulations on the recovery of bank executive compensation.

4.2 Impact on the company's reputation and market value

(1) Impact on the company's reputation

After the Wells Fargo scandal broke out, the most serious impact on the company is the loss of reputation, customers lose trust in Wells Fargo, which is the biggest crisis of trust in the banking industry. Customers believed that the exposed account fraud was just the tip of the iceberg and that Wells Fargo may have more unknown operations and customers were not willing to trust them anymore. Many high-net-worth customers withdrew their deposits from Wells Fargo and switched to other banks, leading to a massive loss of customers. At the same time, many governments ended their relationships with Wells Fargo. The State of California terminated all business with Wells Fargo for a period of one year, including the provision of brokerage services and investment banking. The State of California also refused to purchase Wells Fargo's stock and bonds. The State of Illinois also halted its dealings with Wells Fargo, and the City of Seattle terminated its bond underwriting business. Fitch, one of the three major international rating agencies, downgraded Wells Fargo's rating outlook from "stable" to "negative".

(2) Impact on Market Value

Due to the impact of the Wells Fargo scandal, which resulted in the loss of a large number of customers and the layoff of many basic retail line employees, a decline in performance was inevitable. Firstly, for Wells Fargo, the retail business revenue accounts for half of the total revenue,

and as the main business of Wells Fargo, the dwindling of the retail business will reduce its net profit significantly. Secondly, most of the employees laid off were basic employees in the retail business and it would be difficult to start the business again on a large scale in a short period of time. Community banking business has been a large proportion of Wells Fargo's main business income, and the scandal has had a large negative impact on the operating results of community banking business. Wells Fargo's 2016 annual report data show that its return on total assets was 1.16%, down 0.15 percentage points year-on-year; return on net assets was 11.49%, down 1.11 percentage points year-on-year.

5. Insights and recommendations

5.1 Recommendations for rich countries

(1) Don't set excessive pressure on metrics

Cross-selling has been a successful tool for Wells Fargo. The introduction of cross-selling as a business model set Wells Fargo apart from the rest of the US banking industry and helped it survive the 2008 financial crisis. Cross-selling is measured primarily by the number of products held in the hands of the average customer, which is a direct reflection of Wells Fargo's product penetration. The cross-selling marketing model is more efficient than blindly developing new customers because it seeks to satisfy all of the customer's financial needs and to unlock the customer's value. However, with the changes in the external financial environment and the increase in consumer demand, failure to innovate products in a timely manner may result in the cross-selling model experiencing the phenomenon of marginal effect, i.e., the customer purchasing another product does not enhance the customer's benefit much. If a company is unable to identify these important changes over time and develop reasonable metric requirements, then serious problems can arise.

In 2014, Wells Fargo had reached 6.29 product holdings per capita through cross-selling, a number that will be difficult to continue to increase as the retail market becomes more saturated. Wells Fargo sets product sales targets for its employees on a daily basis, and failure to meet them can result in penalties ranging from minor penalties to dismissal. According to research, before the Wells Fargo scandal broke, basic employees were required to sell at least 8.5 products a day. This was too much to ask of employees, and in a gradually saturated retail market, it was difficult to meet the requirement through normal marketing methods. As a result of the lack of in-depth thinking on cross-selling strategies and setting cross-selling targets too high, employees were forced to find alternative ways to open accounts for customers without authorisation in high-pressure situations.

In recent years, the shortcomings of appraisal metrics have continued to emerge, leading us to the need to reflect on the method. Appraisal indicators are an important tool for achieving business orientation. However, if one relies too much on appraisal indicators and does not abide by the objective laws when setting them and sets too high an indicator, this will lead to employee fraud in order to fulfil the tasks

(2) Change the unreasonable pay incentive mechanism

First of all, the huge pay gap will make the employees psychologically unbalanced, which will affect their motivation to work. After the outbreak of the financial crisis in 2008, Wells Fargo Bank, in order to ensure the continuous growth of profits, constantly lowered the wages of basic employees, while constantly raising the performance index requirements. Before the Wells Fargo scandal, basic employees were required to sell at least 8.5 products per day, and if they could not complete the performance on that day, they would be pushed to the next day, resulting in a backlog of targets and

high sales pressure on employees. At this time, Wells Fargo executives' compensation did not suffer as a result, and Carrie Tolstedt, an executive in the community banking division, was issued $124 million worth of stock by Wells Fargo when she left the company due to the scandal. Former Wells Fargo CEO John Stumpf's annual compensation is even more eye-popping, as shown in the chart below. This huge disparity in pay is bound to affect employees' sense of work ethic.

Second, irrational compensation incentives may lead to short-sighted behaviour by executives, who focus excessively on short-term performance and neglect the bank's long-term stable development. The more aggressive the pay incentive mechanism, the more it will lead to short-sighted behaviour at the top, and the more performance pressure will be exerted on grassroots employees. The original purpose of compensation incentives is to solve the principal-agent problem within the company, so that the interests of the company's shareholders and executives are aligned. However, if performance targets and pay incentives are tightly bound, it will lead to executives being overly concerned about their own interests and resorting to fraudulent behaviours in order to obtain more incentives.

(3) Improve the irrational organisational structure of the company

Wells Fargo's decision-making power is very centralised and there is a lack of balance of power within the company. Before the Wells Fargo scandal broke out, John Stumpf served as both chairman and chief executive officer, and the number of directors within the company was relatively small compared to other companies, which made the power within the company too centralised and the power of all parties could not restrain each other. The board of directors is more concerned about the short-term growth of interests, ignoring the factors of long-term sound development of the bank, blindly pursuing the growth of performance and disregard for the construction and improvement of the internal control system.

If there is no effective supervision of independent directors, as an independent individual, they will put their own interests first. More importantly, even if an independent board of directors is unable to do its job, the punishment for them is limited, which increases the possibility that independent directors will make moves detrimental to the interests of corporate shareholders in pursuit of their own interests.

The essence of the Wells Fargo scandal is a principal-agent problem, where shareholders put the decision-making power in the hands of the board of directors, and appropriate checks and balances should be put in place to prevent directors from pursuing their own interests to the detriment of the bank's long-term development. Set up a supervision department to strengthen daily supervision and management, to achieve prevention and control beforehand, management during the incident, and monitoring after the incident, as well as to improve the internal control system, and effectively strengthen the ability to prevent and control risks.

Conclusion

This paper presents a comprehensive analysis of the Wells Fargo account forgery case, exploring its underlying causes and consequences. By employing stakeholder theory and agency theory, it offers an in-depth study and provides recommendations for the advancement of commercial banks.

Firstly, the paper delves into the reasons behind the forgery case at Wells Fargo. These reasons include an unreasonable performance evaluation system that places undue pressure on employees, leading to unethical behavior; an imperfect corporate governance structure that lacks effective oversight of executives; the challenging external environment faced by the global banking industry;

the formalistic approach to protecting the rights and interests of financial consumers; and insufficient attention and supervision regarding operational risks.

Secondly, using stakeholder theory, the paper examines the far-reaching impact of the Wells Fargo forgery incident. This impact is felt across multiple stakeholders, including shareholders, managers, employees, customers, the entire banking industry, government and regulatory bodies, as well as the bank's reputation and market value. The incident highlights the interconnectedness of these stakeholders and the need for a balanced approach in managing their interests.

Finally, the paper offers recommendations for commercial banks to prevent similar incidents from occurring. These recommendations focus on two key areas: appraisal and incentive mechanisms, and internal control systems. Regarding appraisal and incentives, it is suggested that banks should develop comprehensive evaluation criteria, use cross-selling strategies judiciously, and establish long-term compensation plans. In terms of internal controls, the paper emphasizes the importance of effective checks and balances between the board of directors and management, as well as clearly defined supervisory responsibilities to ensure the effectiveness of multi-layer supervision.

By addressing these issues and implementing the recommended measures, commercial banks can strengthen their operational resilience, enhance stakeholder trust, and ultimately contribute to a more stable and ethical financial industry.

Bibliography

[1] Franco Santos M, Otley D. Reviewing and Theorizing the Unintended Consequences of Performance Management Systems[J]. International Journal of Management Reviews, 2018,20(3):696-730.

[2] Richardson S A, Sloan R G, Soliman M T, et al., 2006“The implications of accounting distortions and growth for accruals and profitability”,. The Accounting Review, 81(3) , pp.713-743.

[3] Knott A., Hayes A., Neslin S. A.. Next-product-to-buy Models for Cross-selling Applications [J].Journal of Interactive Marketing, 2010, 16(3).

[4] Thomas W.Buchner.Performance management theory: A look from the performer's perspective with implications for HRD[J]. Huma Resource Development International, 2007,10(1):59-73.

[5] Ferreira, Santos, Rodrigues. Adding value to bank branch performance evaluation using cognitive maps and MCDA: a case Study[J].Journal of the Operational Research Society, 2011,62(7):1320-1333.

[6] Agrawal A, and S. Chadha,“Corporate governance and accounting scandals”, The Journal of Law & Economics, 48(2)，pp.371-406.

[7] Denisi,Smith,C.E.Performance Appraisal,Performance Management,and Firm-Level Performance:A Review,a Proposed Model,and New Directions for Future Research[J]. Academy of Management Annals,2014,8(1):127-179.

[8] Raffoni A, Visani F, Bartolini M, et al. Business Performance Analytics: exploring the potential for Performance Managemen Systems[J]. Productio Planning&Control, 2018,17(3):1-17.

[9] Armstrong C S, Jagolinzer A D,and Larcker D F. 2010,“Chief executive officer equity incentives and accounting irregularities”,Journal of Accounting Research, 48(2), pp. 225-271

[10] M.A.Barrett.Issues and problems of performance appraisal Systems for university general staff: a study in a U.S.university[J].Journal of Higher Education Policy and Management,2013:152-

[11] Grantham. M, Ross SE, Mackayr, Banfield V, Brown J,Beanlands H. Recruiting and retaining competent clinical nurses[J].Canadian journal of nursing administration, 2013 (8):55-56.

[12] Chidambaran N K, Kedia S and Prabhala N, 2011,“CEO director connections and corporate fraud”, Fordham UniversitySchools of Business Research Paper,NO.1787500.

[13] Debris McGee Wanguri.Cross-Disciplinary Feedback[J].Higher Research on.A Review,Performancean Integration, and a Critique of Appraisals， Evaluations， and Education of Social Science,2014(11): 71-72.

[14] Dechow P M, Ge W, Larson C R, et al.,2011,“Predicting material accounting misstatements”, Contemporary accounting research, 28(1): 17-82.

[15] Alan.Butler,Steve.R.Letza. Linking the balanced scorecard to strategy[J]. Longnge Planning,2008,(30), 242-253.

[16] Andy Neely. Towards the third generation of performance measurement [J].Directorcenter for business performance at cranfield school of management, 2009.

[17] Povel P and Singh R, 2007,“Winton A. Booms, busts, and fraud”,. The Review of Financial Studies, 20(4) , pp.1219-1254.

[18] profitability”,. The Accounting Review, 81(3) , pp.713-743.

[19] Azadeh A, Heydarian D, Nemati K, etal. Performance optimization of unique resilient human resource management system in a coal mine industry[J]. International Journal of system Assurance Engineering&Management, 2018, 9(1):1-20.

[20] Richardson S A, Sloan R G, Soliman M T, et al., 2006“The implications of accounting distortions and growth for accruals and

[21] Ittner,Larcker. Are non-financial measures leading indicators of financial performance? An analysis of customer satisfaction[J].Iournal of accounting research, 2010,(36),152-159.

[22] Kevin.Littler.A new approach to linking strategy formulation and strategy implementation:a example from the UK banking sector[J].International Journal of Information Management,2012,(20),411-421.

[23] Robert.S.Kaplan,David.P.Norton.The strategy focused organization:how balanced scorecard companis thrive in the new business environment[M].Harvard Business School press.2014.

[24] Gregor Virant,Iztok. Implementing a Government-Wide Unified and Transparent salary system in Slovenia [J]. NISPAcee Journal of Public AdminiStration and Policy,2018,11(1).

[25] Shivdasani A, Yermack D,1999,"CEO involvement in the selection of new board members: An empirical analysis", The journal of finance, 54(5),pp. 1829-1853.

[26] Weili Ge, Sarah E.McVay.The disclosure of material weakness in internal control after the Ssarbanes-Ooxley act[U].Accounting Horizons,2005,Vol.19,p.137-158.

[27] Jeffrey Doyle,Weili Ge,Sarah McVay.Determinants of weaknesses in internal control over financial reporting[J]. Working Paper.Journal of Accounting and Economics,2006， Vol.44 (1),pp.193-223.

[28] Andrew Ellul,Vijay Yerramilli.StrongerRisk Controls,Lower Risk: Evidence from U.s.Bank Holding Companies [J].The Journal of Finance.2013,3,(5):371-383.

[29] Dragomir Dimitrijevic,Vesna Milovanovic,Vladimir Stancic,The Role of A Company's Internal Control System in Fraud Prevention[J].e-Finanse,2015.11(3).

[30] KM Zakaria,A Nawawi,ASAP Salin.Internal controls and fraud-empirical evidence from oil&gas conmpany[U].Journal of Financial Crime.2016.23(4):1154-1168.

[31] Hollis Ashbaugh-Skaife ,Daniel W.Collins,William R. Kinney,Jr.， Ryan LaFond， The Effect of Internal Control Deficiencies and Their Remediation on Accrual Quality[J].The accounting review.2008.Vo1.83,No.1 pp.217-250.