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Do Shareholders Penalize Bank Boards and Management for the Financial Crisis?

Do Shareholders Penalize Bank Boards and Management for the Financial Crisis?

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Abstract

The 2007-2008 financial crisis was a pervasive shock that profoundly impacted the financial services industry. Often described as the worst economic crisis since the Great Depression, this event provides a unique opportunity to examine the consequences experienced by members of boards of directors and top management at bank holding companies for what shareholders may perceive as failures in oversight and excessive risk-taking. This study examines whether shareholders penalized top management at banks and provides some new evidence of the crisis's impact on management careers. Using the 36 largest American bank holding corporations by assets as a sample, we examine director re-election percentages and other director, management, and firm characteristics to determine the extent to which shareholders indicate their disapproval of banks' boards of directors during and after the financial crisis. By employing various methods of empirical analysis, including ordinary least squares regressions, two-sample t-tests, and Wilcoxon rank-sum tests, we have determined with statistical confidence that the average number of shareholder votes in favor of bank director nominees decreased significantly at the end of and in the years immediately following the financial crisis. Further, we find that much of this decrease in shareholder approval can be attributed to several firm, board, and director-specific characteristics. These results have important corporate governance policy implications and may suggest additional avenues of exploration regarding this or other such industry-wide or macroeconomic crises.

I. Introduction

The 2007-2008 financial crisis is often attributed to failures of oversight and excessive risk-taking on the part of bank holding companies in the United States and around the world. Politicians, the media, and members of social movements like Occupy Wall Street, for example, accuse the leadership of major domestic banks of not being held sufficiently responsible or penalized for their perceived role in precipitating the crisis. U.S. President Barack Obama, in a news conference on Thursday, October 6, 2011, said of this perception, "You're still seeing some of the same folks [bankers] who acted irresponsibly trying to fight efforts to crack down on abusive practices that got us into this problem in the first place" (Salazar and Zraick, 2011). A thorough investigation of the consequences actually experienced by the leaders of the American financial services sector following the crisis may therefore inform these continuing conversations and yield important policy implications.

The history of the financial crisis provides insight into the need for such a study. Yeoh (2009) provides a helpful summary of the event. The origin of the crisis is traced to late 2006 and early 2007, when housing prices in the United States experienced a sudden and dramatic decline. This collapse in turn prompted several banks in the United States and Europe, especially those with high exposure to the property markets, to post significant losses (Yeoh, 2009, pp. 42-43). Such exposure came in the form of exotic financial instruments that packaged "toxic" subprime mortgage securities with less risky assets (Yeoh, 2009, p. 49). These instruments, despite their risky components, were marketed with favorable triple-A risk ratings, giving investors a false sense of security. Such financial instruments are now heavily regulated (Austill, 2011, p. 66). Thus, the collapse of the housing and debt markets precipitated substantial and unforeseen financial losses for investors, banks, and governments across the world. The United States thereafter entered into an economic recession in late 2008, and although economic conditions have technically improved somewhat since then, the life savings of many individuals has yet to be recovered (Yeoh, 2009, p.43). Yeoh (2009) also observes that regulators, investors, and policy-makers were very concerned with failures in the governance of banks, especially in the wake of "emerging [accounts of] corporate misconduct and extreme corporate adventurism in these failed and failing institutions" (p. 54). Despite these perceived indiscretions on the part of bank leadership, financial institutions such as American International Group (AIG), Fannie Mae,

and Freddie Mac, among others, received controversial bailout funding or other special assistance from the U.S. federal government (Yeoh, 2009, p. 50). Many banking executives were simultaneously awarded large severance packages in exchange for resigning from their respective firms. Yeoh (2009) asserts that the issue of bank executive compensation could be among "the most important corporate governance failure[s] of the subprime crisis," one that may have been triggered in part by "directors' failure to effectively challenge" the lavish pay structure of their firms' chief executive officers (Yeoh, 2009, 58).

Accordingly, it is clear that many people, from scholars to President Obama, do not perceive the professional consequences experienced by bank leadership as commensurate with the negative effects of the financial crisis and economic recession experienced by society as a whole. During the crisis, many high-profile firings of CEOs and other matters of bank leadership and corporate governance were the subject of countless media inquiries (e.g., Keoun, 2007; Berman, 2008; and Reckard, 2009). Now that the economy of the United States is beginning to recover, it is possible to examine consequences experienced by bank boards and management during the crisis with the benefit of hindsight. Several studies about the nature of director elections and their implications for management and firm performance (e.g., Cai, Garner, and Walking, 2009; Kirkpatrick, 2009; and Hermalin and Weisbach, 2003) will inform such an effort.

II. Literature Review

The existing literature on the topic of governance of large corporations suggests that the issues explored in this study are timely. Preston (1990), for instance, observes a positive relationship between the size of an organization and societal perceptions of social responsibility (p. 369). The top 36 publicly traded American bank holding companies examined in this study own approximately $13 trillion in assets—a figure that is quickly approaching the same amount as the United States' annual gross domestic product—and serve as the backbone of the American and global credit markets. Justifiably or not, the public expects firms of extraordinary size to wield their influence responsibly, and so may hold such firms responsible for poor macroeconomic performance. Nonetheless, large firms such as these typically have complex operations; they are more challenging to oversee, manage, and control from a governance perspective (Zahra and Pearce, 1989,

p. 294). How, then, are the shareholders or owners of these firms to ensure effective governance?

The answer is found with the firm's board of directors. Regulation in the United States requires that all publicly traded companies be overseen by a board of directors elected by the shareholders. Hemalin and Weisbach (2003) describe a firm's board as the "equilibrium solution" to the agency problem that exists between the firm's shareholders and managers (p. 10). In this view, because shareholders directly elect the members of the board, directors act as agents of the shareholders. The board, on behalf of shareholders, oversees firm management by providing incentives for executives to act in certain ways (Cai, Garner, and Walkling, p. 2389). By law, boards must consist of a minimum number of individuals, meet regularly, form committees, and comply with various rules regarding group composition (Hemalin and Weisbach, 2003, p. 9). Thus, boards exist both to optimize organizational design and to comply with regulations. Such regulations exist, in theory, to protect shareholders and the market at large.

Typically, boards fulfill several roles in the governance of firms. First, they provide advice and counsel to top management (Adams, Hermalin, and Weisbach, 2010, p. 64). In this sense, directors are appointed because they possess a particular level of expertise or outlook that would add value to the firm. Directors are therefore charged with determining the strategic direction, mission, vision, and corporate policies of the firm, and providing leadership during crisis situations (Adams, Hermalin, and Weisbach, 2010, p. 64). Finally, boards of directors serve a disciplinary role for the firm in that top management, along with all firm employees, is held accountable to the board (Adams, Hermalin, and Weisbach, 2010, p. 64).

One of the most important responsibilities of a board of directors is to change the firm's chief executive officer (CEO), if necessary. Firms' boards are tasked with monitoring the abilities and actions of top management, continually assessing the value and quality of each (Adams, Hermalin, and Weisbach, 2010, p. 65). When the firm does not perform to the shareholders' expectations, the board is responsible for intervening, and, in many cases, replaces the CEO. Hemalin and Weisbach (2010) observe a strong positive correlation between poor firm performance and board-induced CEO turnover (p. 14). In scenarios such as these, board composition plays an important role in the rate of CEO turnover. Typically, board composition is examined in terms of the ratio of insider directors to independent directors. Insider directors are those directors who concurrently serve or have previously served as

officers or employees of the firm they govern, and are viewed as more sympathetic to the CEO. Independent directors have no such ties to the firm, and are perceived as more inclined to replace the CEO and other top managers in the wake of poor performance. In a board dominated by insiders, however, CEO turnover decisions are somewhat unrelated to firm performance (Hermalin and Weisbach, 2010, p. 11). The insider-outsider ratio is also not correlated with firm performance as a whole (Hermalin and Weisbach, 2010, p. 12). Ultimately, the effectiveness of the board at monitoring firm performance is determined by the board's independence, size, and composition (John and Senbet, 1998).

Boards tend to do their work in committees. The board members, often in conjunction with the CEO, determine who among them will serve on each board committee. The audit committee assures the integrity of the firm's financial statements, oversees the firm's accounting procedures, and maintains compliance with relevant laws, policies, and regulations that pertain to the firm. Directors on the compensation committee determine the pay, stock options, and other benefits awarded to firm employees, especially top management. The risk committee oversees CEO and top management responsibilities as they pertain to credit, market, interest rate, investment, liquidity, and reputational risk. Finally, a nominating, or governance, committee updates the firm's corporate governance policies and nominates additional members to the board of directors. Each bank in this study generally has at least three of the four aforementioned board committees.

The nominating committee is particularly important to this study, both because of its relationship to the CEO and because its decisions indirectly determine the efficacy of the board by deciding who will join the board when vacancies arise. Cai, Garner, and Walkling (2009) observe that this committee is consequently often subject to the "dramatic influence" of the CEO, who has a vested interest in filling the board with friendly, insider directors (p. 2392). According to Adams, Hermalin, and Weisbach (2010), CEOs prefer an insider board, while the board itself prefers independence from the CEO (p. 66). This is because a CEO with an insider board is better positioned to negotiate for higher pay or to ensure job security in the event of poor firm performance; independent boards, on the other hand, have little incentive to deviate from objectively monitoring firm performance. The nominating committee also routinely nominates incumbent directors for CEO (Adams, Hermalin, and Weisbach, p. 66).

Nominees to the board are submitted to shareholders for a vote once per year. Each nominee must receive a plurality of shareholder votes

in order to be seated on the board. Because nominating committees and CEOs have no incentive to nominate multiple individuals for the same director position, virtually all director nominations are uncontested (Cai, Garner, and Walkling, 2009, p. 2392). Votes may be cast for a director, withheld from a director, or not cast at all. In the United States, there is no mechanism for shareholders to cast "votes against" nominees (Cai, Garner, and Walkling, 2009, p 2396). Thus, the plurality voting system inherently weakens the strength of shareholders, as not voting for a nominee essentially does nothing; a nominee in an uncontested director election requires only one vote to win (Cai, Garner, and Walkling, 2009, p. 2390).

Therefore, securing a nomination to the board almost inevitably ensures victory in the shareholder election. In practice, shareholders have very limited ability to remove directors from the board, to propose their own director nominees, or to deny nominees from assuming office. Because of the nomination and plurality system, incumbent directors "do not currently face any meaningful risk of being replaced" by shareholder vote (Bebchuk, 2003, p. 1). Cai, Garner, and Walkling (2009) also observe that incumbent directors generally always win re-election when re-nominated. A 90% margin of victory in the re-election vote is the norm, even for poorly performing directors. This presents a significant corporate governance problem: even though directors are the agents of the shareholders, the shareholders are generally not empowered to remove directors or to select or veto director-nominees.

Nonetheless, shareholders may communicate their disapproval of poorly performing directors and firms by refusing to vote in favor of director-nominees. As per the rules of plurality, nominees are still seated on the board even though they may receive a low percentage of shareholder votes in favor. However, lower margins of victory are still undesirable for directors, as such outcomes may result in negative publicity or embarrassment to individual directors or to their firms (Cai, Garner, and Walkling, 2009, p. 2389).

Director turnover is desirable for shareholders, especially when firms perform poorly. A study conducted by Schnake, Fredenberge, and Williams (2005) found a negative correlation between board member tenure and firm misconduct as a product of poor corporate governance (p. 103). Long-tenured board members may, with time, become too comfortable with the organizational status quo, thereby losing their ability or inclination to recognize and respond to problems within the firm. This finding also reinforces the notion that independent directors are best equipped to objectively govern a firm.

The frequency with which board members are subject to shareholder re-election depends on whether a board is classified or declassified. Classified boards are those with staggered director elections. On such boards, only a portion of the directors—usually one-third—are up for election each year (Cai, Garner, and Walkling, 2009, p. 2392). Classified boards are effective at preempting takeovers in that they require dramatic changes in firm leadership to take place over several years. By contrast, all members of declassified boards of directors must be re-elected each year by shareholders. Declassified boards are, by definition, more accountable to shareholders, as they must secure re-election every year (Cai, Garner, and Walkling, 2009, p. 2411).

The aforementioned theories about fundamental governance inform this study's examination of shareholder sentiment and subsequent director response during the financial crisis. Kirkpatrick (2009) concludes that the financial crisis can be attributed in part to "failures and weaknesses in corporate governance arrangements which did not serve their purposes to safeguard against excessive risk taking in a number of financial services companies" (p. 61). Similar failures in board effectiveness have been observed throughout recent history with firms like Enron, WorldCom, Ahold, and Parmalat. Specifically, Kirkpatrick (2009) blames the banks' boards for ignoring warnings issued by the International Monetary Fund and the Bank of England regarding rising mortgage default rates, while simultaneously allowing their firms to make widespread use of toxic mortgage-backed securities in order to boost profits (p.64). Many banks' boards of directors also failed to restrict management from hiding losses through off-balance-sheet accounting practices permitted by loopholes in Basel I regulations (Kirkpatrick, 2009, p. 65).

Kirkpatrick (2009) establishes that failures in governance on the part of boards of directors of bank holding companies may have triggered, if not caused, the financial crisis. In theory, these directors' actions ought to have been guided by the will and the best interests of shareholders; by definition, directors are agents to the shareholders' principals. Determining whether shareholders blame or penalize bank directors and management for the financial crisis may therefore determine the extent to which this agency problem existed during the event and, further, may lead to the creation of new policies that could prevent another crisis from occurring. Despite the potential benefits of such an endeavor, there has yet to be a comprehensive event study of shareholder sentiments toward the leadership of bank holding companies during the financial crisis.

This study examines shareholder votes for nominees to the boards of directors of bank holding companies to determine whether and why shareholders penalize the boards for the financial crisis. Cai, Garner, and Walkling (2009) have demonstrated the effectiveness of this method at predicting correlations between vote margins and board actions; indeed, this study makes use of an updated version of the Institutional Shareholder Services director election data used by Cai, Garner, and Walkling (2009). Additionally, many studies on firm performance and boards of directors (e.g., Cai, Garner, and Walkling [2009]; John and Senbet [1998]; Zahra and Pearce [1998]) are not industry specific, nor were they conducted in response to a large, macro-level event such as the financial crisis. Schnake, Fredenberger, and Williams (2005), however, successfully examined board composition and firm misconduct in the financial services sector in a study that predates the financial crisis, demonstrating that the approach used in this study is both appropriate and timely. Indeed, it may be possible to extrapolate the findings of this study to other firms or industries experiencing similar pervasive economic shocks.

III. Hypotheses

The hypotheses tested in this study are informed by the aforementioned literature, especially Cai, Garner, and Walkling (2009), who recently conducted a comprehensive study of uncontested director elections across all industries and found that even poorly performing directors receive at least 90% favorable votes in regard to their nominations. These authors also find that directors of poorly performing firms receive a statistically significantly lower percentage of votes for re-election. As virtually all of the major American bank holding companies suffered decreases in profits, or losses, during the financial crisis, our study seeks to determine the extent to which shareholders attributed banks' poor performance to their respective boards of directors. In this study, shareholders are therefore assumed to disapprove of a director when fewer than 90% of votes cast in that election comprise "votes for" the director. We therefore expect director approval, as measured in terms of this "votes for" percentage, to decline each year beginning in 2007. In order to best capture the opinion of shareholders during and after the financial crisis, we study this phenomenon in each year from 2007 to 2010, using 2006 as a benchmark year.

> H_{1a}: Shareholders of bank holding companies signaled their dissatisfaction by re-electing director-nominees by statistically significant lower percentages over time during the financial crisis, beginning in 2006 and declining each year through 2010.

During the crisis, for instance, shareholders may have been more reactionary or concerned with firm preservation. By contrast, shareholders may have been more contemplative or under less pressure to retain directors once the economy began to stabilize in 2009 and 2010, especially with the benefit of hindsight. It is also noted that complete data for fiscal year 2011 does not yet exist in time for this study, as firms submit DEF-14A proxy statements to shareholders and the Securities and Exchange Commission in March or April of the following year.

In addition, we are also interested in comparing director election results for banks versus non-banks during the same time period. The financial crisis affected the value of virtually all publicly traded firms in the United States. However, because current literature in this field attributes the crisis itself to excessive risk-taking and governance failures at financial services institutions, we further hypothesize that shareholders of banks disapproved of their directors to a greater degree than did shareholders of non-banks with respect to their own directors. The results of this hypothesis will allow us to determine whether lower bank director vote percentages, if they occurred, were unique to the financial services industry.

> H_{1b}: Bank directors received statistically significant lower re-election percentages versus their colleagues on non-bank boards during the financial crisis, beginning in 2006 and declining each year through 2010.

Furthermore, if bank shareholders did in fact disapprove of incumbent directors' performance, the outcome of each election may be predicted by the characteristics of each nominee or the state of the firm or the firm's board. The aforementioned literature suggests that shareholders are typically deliberate and thoughtful when casting their votes for directors during periods of crisis. For example, shareholders may have been more likely to vote against incumbent directors who were in charge during the financial crisis (a period of drastically poor firm performance), or those with comparatively longer board tenures or membership on important board committees. Additionally,

shareholders may have penalized directors on classified boards or certain board committees, or directors with particular professional or academic backgrounds. They also may have penalized directors when the firm's stock price decreased since the previous director election. Such a scenario would imply that shareholders may have taken these characteristics into account when casting their votes in director elections.

> H_2: Individual bank director election outcomes during the financial crisis were determined by firm, board, and individual nominee characteristics.

IV. Methodology and Data

The sample of banks chosen for this study begins with the United States Federal Reserve's list of the top 50 domestic bank holding companies by assets, which is publicly available and continuously updated on the Internet. Twelve banks that are not publicly listed and those that are not domiciled in the United States were excluded from the sample, both to control for regulations and governance standards, as well as to ensure a uniform dataset. Finally, we excluded two banks for which director election vote data was unavailable from Institutional Shareholder Services, for a total of 35 firms. Together, these firms control approximately $13 trillion in assets ("Top 50 Banks," 2012).

Institutional Shareholder Services (ISS) provided data on the votes cast in individual director elections from 2006 to 2010 for 1,882 publicly traded firms. This data includes firm name; director name; vote margin requirement; election date; total outstanding shares; and total votes cast for, withheld, and in abstention. We extracted from this dataset the aforementioned 36 banks (1,673 separate bank director elections) chosen as the study's sample for hypotheses H1a and H2. Hypothesis H1b compares the sample of 36 banks to the remaining 1,857 non-banks (42,928 separate non-bank director elections) for which director election data is also available. The time period in question for this study is 2007 to 2010, with 2006 as the benchmark year. A complete list of each bank used in this study is included in *Figure 1: Sample of the Top Public American Bank Holding Companies.*

Information regarding director characteristics was manually collected from DEF-14A "Definitive Proxy Statements," which are posted for public access on the Security and Exchange Commission's Internet-

based EDGAR database. These statements are sent to shareholders each year ahead of annual shareholder meetings, and shareholders are able to submit their votes on various issues, including director elections, back to the firm by ballot if they are not able to attend the meeting in person. This newly collected data was accordingly added to the director election data from ISS. We also collected data regarding CEO and board turnover from DEF-14A statements in order to get a complete, descriptive understanding of changes in firm leadership during and after the financial crisis. A summary of this data is presented in *Figure 2: Overall Average Board Turnover; Figure 3: Overall Average Board Size; Figure 4: CEO Turnover by Year; and Figure 5: Director Turnover by Board Type (see Appendix I).*

Each bank's stock price on the day of the shareholder meeting to elect directors was collected from *Yahoo! Finance*. We calculated the change in the stock price from the previous election, and added this information to each item of director election data from ISS. We further plotted these stock prices against the aforementioned data regarding board turnover and changes in board size, both for individual firms and the entire sample of 36 banks. These charts suggest that during the financial crisis there may have been a negative correlation between stock price (as a proxy for firm performance) and board turnover. Again, these descriptive statistics reinforce the methodology behind our hypothesis formulation, and suggest that other firm, board, or director-specific variables may have influenced shareholders' votes. A synopsis of average changes in our sample firms' stock prices and board changes can be found in *Figure 6: Stock Price vs. Board Changes* in Appendix I.

To further enhance our descriptive analysis, this study collects data on director, CEO, and top management compensation packages from the Wharton Research Data Services (WRDS) ExecuComp database. Compensation amounts are listed as fair market values and are sorted into various categories, including salary/cash, bonus, stock, options, pension, and restricted shares. The sum of all categories is also taken. This data was collected in the event that it might prove useful in the formulation of additional hypotheses pertaining to director votes and changes in compensation. We observe that directors and top managers alike experienced a sharp decrease in compensation during the financial crisis, suggesting that they may have been penalized in other, non-financial ways, including in terms of election percentages. Summaries of this data are presented in Appendix I, and include *Figure 7: Bank Director Compensation; Figure 8: Top Management Compensation; and Figure 9: Bank CEO Compensation.*

We used Stata 12, a statistical analysis program, to test our hypotheses. In order to test for statistical differences in mean and median shareholder vote percentages in H1a and H1b, we run two-sample t and Wilcoxon rank-sum tests, respectively.

To determine which firm, board, and director characteristics contributed to the percentage of votes cast in favor of director nominees, if any (H2), we run ordinary least squares (OLS) multiple regressions.

V. Data Analysis and Potential Contributions

This study examines 1,673 bank director elections from 2007 to 2010 on both classified and non-classified boards, using 2006 as a benchmark year. The distribution of the elections, by year and board type, is summarized in Table I.

Table I: Sample of bank director elections by year and board type

This table lists the number of bank director elections for each year in this study. Column two lists the number of director elections on non-classified boards, and column three lists the number of elections on classified boards, with a total in column 4.

	Non-Classified	Classified	TOTAL
2010	324	42	**366**
2009	287	67	**354**
2008	272	62	**334**
2007	258	77	**335**
2006	212	72	**284**
TOTAL	**1353**	**320**	**1673**

Of the 476 individual bank directors in this study between 2006 and 2010, 146 directors were replaced, thereby implying a 30.6% turnover rate across these five years. Toward the end and after the financial crisis, directors of non-classified boards tended to be replaced at an increasingly faster rate, while the opposite trend is observed for bank directors on classified boards, as seen in Table II. However, the decrease in the classified board director turnover rate after the

financial crisis can probably be attributed to the fact that many boards elected to declassify themselves—effectively making the boards more accountable to shareholders but subjecting themselves to more frequent elections—during and after the event. Indeed, if a director on a classified board received less than 90% of the vote for election during a particular year, that director's board declassified itself later that year 12% of the time. Of the 19 classified bank boards in our sample at the beginning of 2006, nine of them eventually declassified themselves by the end of 2010. Similarly, if a director received less than 90% of the vote for election during a particular year, that director's board size decreased later that year 25% of the time. A decrease in board size, as previously mentioned, is generally considered advantageous to shareholders, as smaller boards tend to be more accountable and active monitors of firm performance. Table II describes the distribution of instances of bank director turnover.

Table II: Instances of bank director turnover

This table describes the number of times an incumbent bank director was not renominated despite being eligible for renomination each year. The results are separated by board classification type. The first column of each classification category indicates the number of such directors, while the second column expresses that number as a proportion of the total number of director elections that took place during the previous year.

Year	Non-Classified		Classified		Total	
	Number	%	Number	%	Number	%
2010	32	10%	2	1%	34	9%
2009	35	12%	8	2%	43	12%
2008	30	11%	8	2%	38	11%
2007	15	6%	16	5%	31	9%
2006	15	7%	14	5%	29	10%
TOTAL	127	9%	48	15%	175	10%

It is worth noting that not one of the 1,673 bank director elections in this study resulted in the failure of a nominee to secure election at the hands of shareholders. Nominees were withdrawn in only two separate instances (before shareholders could cast their votes). Further, the votes of 11 CIT Group Inc. director elections were not disclosed. Otherwise, all bank director nominees were elected.

Table III lists the number of times director-nominees, both from the bank sample and from all other firms in the larger population, were elected with fewer than 90% of votes cast in favor, indicating shareholder disapproval. These descriptive results from Table III indicate that shareholders strongly disapproved of bank board members during and after the financial crisis; hypothesis H1 will test to determine whether these changes in approval are statistically significant. To reiterate, in this study, shareholders are assumed to disapprove of directors when fewer than 90% of votes cast in a director election comprise "votes for" the director.

Table III: Instances of shareholder disapproval of directors (banks and all other firms)

This table describes the number of times directors were elected with fewer than 90% of votes cast in favor, and are separated first by banks and non-banks, and then by board classification type. For each classification type, column 1 counts the number of times shareholders received less than 90% of the votes cast in favor, and column 2 lists that number as a percentage of the total director elections that took place during that year.

Year	Banks in Sample						All Other Firms	
	Non-Classified		Classified		Total		Total	
	Number	%	Number	%	Number	%	Number	%
2010	249	77%	30	8%	279	76%	5,473	60%
2009	48	17%	13	4%	61	17%	1,776	20%
2008	41	15%	8	2%	49	15%	1,193	14%
2007	14	5%	2	1%	16	5%	1,049	13%
2006	12	6%	5	2%	17	6%	786	10%
TOTAL	**364**	**27%**	**58**	**18%**	**422**	**25%**	**10,277**	**24%**

This study also observes 23 instances of a bank in our sample changing its CEO between 2006 and 2010; therefore, 56% of the CEOs in this study's sample of bank holding companies lost their jobs during or after the financial crisis. Summaries of this data are presented in Apendix I, and include *Figure 2: Overall Average Board Turnover; Figure 3: Overall Average Board Size; Figure 4: CEO Turnover by Year; and Figure 5: Director Turnover by Board Type.* Table IV illustrates how many CEOs retained their positions between given years during and after the financial crisis; less than half of the individual CEOs who were managing our sample's 36 banks in 2007 retained their positions by the beginning of 2011.

Table IV: Number of bank CEOs who retained their jobs from Year Y to Year X

This table lists the number of times a CEO who was in office at the end of the shareholder election meeting in Year Y retained his or her job by the same time in Year X. The results are separated by year. For each year, the number of CEOs to retain their positions is listed in column 1. Column 2 expresses this number as a proportion of the number of individual CEOs who were in office during Year Y. As an example, 24, or 64.8%, of the CEOs in 2007 retained their position by the shareholder election meeting in 2010. There are 37 CEOs across the 36 banks in our sample; Hancock Holding Company has two co-CEOs.

Year Y	Year X							
	2008		2009		2010		2011	
	Number	Percent	Number	Percent	Number	Percent	Number	Percent
2007	31	83.8%	26	70.3%	24	64.8%	17	45.9%
2008	-	-	32	86.5%	29	78.3%	21	56.8%
2009	-	-	-	-	34	91.9%	26	70.3%
2010	-	-	-	-	-	-	28	75.7%

The results of testing hypothesis H_1

Hypothesis H_{1a} asserts that the percentage of shareholder votes cast in favor of bank director nominees decreased in a statistically significant way during and after the financial crisis. Specifically, we seek to determine whether affirmative vote percentages decreased beginning in 2007 through 2010 relative to 2006. In order to test this hypothesis, we run a separate two-sample, one-tail t-test for each of the sample means for each time period in question, using the mean proportion of votes cast in favor from 2006 as a benchmark. This method tests whether the actual mean for each given time period is statistically less than the benchmark year's mean in 2006. Table V summarizes the results of each t-test.

Table V: Bank director nominee affirmative vote percentage: two-sample t-test

This table lists the results of a two-sample t-test to determine whether the mean proportion of votes cast in favor of all bank director-

nominees for each year is statistically less than the same metric in the base year (2006). Column 2 lists the number of bank director elections in the given year. Column 3 describes the mean proportion of votes cast in favor. The subsequent three columns list the p-value for each difference of means, where column 4 tests whether the mean of the year in question is statistically greater than the benchmark year; column 5 tests whether the mean of the year in question and that of the benchmark year are statistically equal; and column 6 tests whether the mean of the year in question is statistically less than the benchmark year. A p-value below 0.01 indicates significance at the 1% level.

Year	Observations	Vote For % Mean	Ha: diff < 0 p-value	Ha: diff = 0 p-value	Ha: diff > 0 p-value
2010	365	0.8459	1.0000	0.0000	0.0000
2009	354	0.9316	1.0000	0.0000	0.0000
2008	322	0.9482	0.9970	0.0059	0.0030
2007	335	0.9591	0.6332	0.7336	0.3668
2006	284	0.9604	-	-	-

The small p-values of each t-test enable us to accept H1a for 2008, 2009, and 2010. Directors of American banks during those years experienced a statistically higher rate of shareholder dissatisfaction when they ran for election or re-election.

Additionally, we run a two-sample Wilcoxon rank-sum test to determine whether the differences between median affirmative vote means are statistically significant, as summarized below in Table VI

Table VI: Bank director nominee affirmative vote percentage: rank-sum test for median difference

This table reports data on the average percentage of votes cast in favor of the bank director-nominee for each year from 2007 to 2010. The second column reports the number of bank director-nominees elected each year and the third column reports the average percentage votes in favor of the nominee. Column four reports the Wilcoxon-z rank-sum score testing for a difference in the median between the percentage of votes in favor in the year compared to the average votes cast in favor of bank nominees in 2006, two years prior to the crisis year. The last column reports the p-values of the rank-sum test column; p-values below 0.01 indicate significance at the 1% level.

Year	Observations	Vote For % Mean	z	Prob. > |z|
2010	365	0.8459	17.845	0.0000
2009	354	0.9316	6.645	0.0000
2008	322	0.9482	3.610	0.0003
2007	335	0.9591	3.230	0.0012
2006	284	0.9604	-	-

The differences between median affirmative vote means are statistically significant for each year, confirming our decision to accept H_{1a}. We therefore conclude that bank directors received statistically fewer proportions of affirmative votes both during and after the financial crisis for 2008, 2009, and 2010.

H_{1b} asserts that bank directors received statistically significant lower re-election percentages versus their colleagues on non-bank boards during 2007, 2008, 2009, and 2010. We run the same t-tests to test the differences between mean votes in favor of bank directors versus non-bank directors, using 42,928 director elections across 1,873 other publicly traded firms from 2006 to 2010 as our sample for the latter. The results are summarized in Table VII.

Table VII: Bank director-nominee affirmative vote percentages, banks vs. non-banks

This table compares the average percentage of votes cast in favor of bank director-nominees for each year with the same metric for non-bank directors in our sample. Columns 2 and 4 list the number of bank and non-bank director elections, respectively. Columns 3 and 5 display the average percentage of votes cast in favor of bank directors and non-bank directors, respectively. The subsequent columns list the p-values for tests for statistical differences between these two means. Column 4 tests whether the mean for bank directors is statistically less than the mean for non-bank directors; column 5 tests whether there is no statistical difference between the two means; and column 6 tests whether the mean for bank directors is statistically greater than the mean for non-bank directors. A p-value below 0.01 indicates significance at the 1% level.

Year	Observations (Banks)	Vote For % Mean	Observations (Non-Banks)	Vote For % Mean	Ha: diff < 0 p-value	Ha: diff = 0 p-value	Ha: diff > 0 p-value
2010	365	0.8459	9,195	0.8543	0.9277	0.1446	0.0723
2009	354	0.9316	8,975	0.9244	0.1347	0.2694	0.8653
2008	322	0.9482	8,523	0.9454	0.2637	0.5273	0.7363
2007	335	0.9591	8,029	0.9482	0.0050	0.0100	0.9950
2006	284	0.9604	7,744	0.9603	0.0316	0.0632	0.9684

We therefore observe that shareholders of non-banks approved of their directors more than did shareholders of banks during 2006 and 2007, before the financial crisis. However, during and after the financial crisis (2008 to 2010), we cannot conclude with statistical confidence whether the means of shareholder votes in favor for director nominees was different. H1b is therefore rejected.

The results of testing hypothesis H_2

Hypothesis H_2 asserts that the percentage of shareholder votes cast in favor of bank director-nominees during the financial crisis can be accurately predicted based upon certain firm, board, or individual director characteristics. Several of the descriptive statistics previously mentioned, as well as current literature in this field, inform our decision to incorporate the independent variables used in the multiple regressions to be used to test for these relationships. For example, as displayed in Tables VIII, IX, and X, committee membership and board tenure may have been a factor in board turnover and shareholder disapproval of directors.

Table VIII: Bank director turnover by committee membership

This table describes the distribution of bank director turnover by board classification type and committee (audit committee, compensation committee, and government committee) for each year. A bank director is said to have "turned over" if he or she was not renominated, despite being eligible, during each year in question.

Year	Non-Classified Boards			Classified Boards			
	Audit	Compensation	Nominating	Audit	Compensation	Nominating	TOTAL
2010	11	3	6	2	4	1	27
2009	8	8	9	4	4	7	40
2008	10	5	8	1	3	3	30
2007	4	9	7	4	4	5	33
2006	12	8	12	2	2	2	38
TOTAL	45	33	42	13	17	18	168

Table IX: Average consecutive board tenure of retiring bank directors by committee membership

This table is an extension of Table VIII and displays the average tenure of the bank directors on each committee at the time of their separation from the board. Only directors who have "turned over" are counted toward this average. A bank director is said to have "turned over" if he or she was not renominated, despite being eligible, during each year in question.

Year	Non-Classified Boards			Classified Boards			
	Audit	Compensation	Nominating	Audit	Compensation	Nominating	AVERAGE
2010	10.5	13.3	8.7	3.0	7.5	0.0	**7.2**
2009	9.5	8.5	10.9	14.8	8.8	11.7	**10.7**
2008	5.7	7.4	9.5	1.0	8.0	8.0	**6.6**
2007	12.0	7.0	7.6	7.5	13.3	11.4	**9.8**
2006	11.0	6.3	9.9	14.0	3.0	3.0	**7.9**
AVERAGE	**9.7**	**8.5**	**9.3**	**8.1**	**8.1**	**6.8**	-

Table X: Number of unpopular bank directors (<90% shareholder support) by board committee

This table is an extension of Table VIII and displays the number of unpopular bank directors on each committee during the given year. A director is said to be "unpopular" or "disapproved of" by shareholders if he or she received less than 90% of the votes cast in favor of his or her nomination to the board during that year.

Year	Non-Classified Boards			Classified Boards			
	Audit	Compensation	Nominating	Audit	Compensation	Nominating	TOTAL
2010	22	23	21	5	4	6	**81**
2009	13	21	19	9	3	7	**72**
2008	23	15	23	2	5	4	**72**
2007	27	17	24	3	1	4	**76**
2006	17	19	14	1	2	2	**55**
TOTAL	**102**	**95**	**101**	**20**	**15**	**23**	**356**

Accordingly, the independent variables included in the testing of this hypothesis include the following about each director nominee, where applicable: board tenure in years; whether the nominee was in office during the financial crisis (2007 or 2008); committee membership (audit, governance, and/or nominating committees); whether or not the board

was classified at the time of the election; the percent change in the firm's stock price since the previous director election; whether the nominee had any prior experience in business or the financial services industry; whether the nominee had previously served as a CEO, CFO, or director of a firm; the number of previous directorships the nominee had held; special professional experience (as an academic, a legal professional, or an elected or appointed member of the government); and whether the nominee was determined to be "independent" of the firm, as per SEC law.

Several models are proposed in our OLS regressions below. Model 1 takes into account only firm performance and director tenure characteristics. Model 2 is an expansion of Model 1 and includes director-nominee board committee membership, as well as whether or not the board is classified. Model 3 is also an expansion of Model 1, and includes director professional and educational characteristics. Model 4 is a combination of Models 2 and 3, and Model 5 includes year effects. These various models allow us to partially accept H2 on the basis of the multiple regression analysis presented in Table XI.

Table XI: Multiple regression analysis of the percentage of votes in favor of bank directors

This table shows the results of a multiple ordinary least squares regression analysis of the percentage of votes in favor of the bank director-nominee. The dependent variable is the average percent of "for" votes of all directors being elected in a bank for each year. The independent variables are board tenure in years; whether the nominee was in office during the financial crisis (2007 or 2008); committee membership (audit, governance, and/or nominating committees); whether or not the board was classified at the time of the election; the percent change in the firm's stock price since the previous director election; whether the nominee had any prior experience in business or the financial services industry; whether the nominee had previously served as a CEO, CFO, or director of a firm; the number of previous directorships the nominee had held; special professional experience (as an academic, a legal professional, or an elected or appointed member of the government); and whether the nominee was determined to be "independent" of the firm, as per SEC law. Appendix II defines each independent variable in greater detail. Various regression models are shown, with coefficients in bold and p-values in parentheses. *, **, and *** denote statistical significance at the 10%, 5%, and 1% levels, respectively.

Independent Variables and Statistics	Dependent Variable = Average Percent "for" Votes				
	(1)	(2)	(3)	(4)	(5)
Board Tenure	-0.001 (0.000)***	-0.001 (0.000)***	-0.001 (0.000)***	-0.001 (0.000)***	-0.001 (0.010)***
Director During Crisis	0.076 (0.000)***	0.070 (0.000)***	0.076 (0.000)***	0.070 (0.000)***	0.018 (0.024)**
% in Current Stock Price	-0.027 (0.000)***	-0.027 (0.000)***	-0.027 (0.000)***	-0.027 (0.000)***	0.023 (0.000)***
Independent Director	-0.014 (0.005)***	-0.012 (0.016)**	-0.014 (0.010)***	-0.012 (0.024)**	-0.008 (0.061)*
Audit Committee		0.000 (0.924)		-0.002 (0.579)	-0.005 (0.207)
Compensation Committee		0.003 (0.506)		0.002 (0.612)	0.007 (0.070)*
Nominating Committee		0.003 (0.530)		0.003 (0.524)	0.000 (0.933)
Classified Board		0.014 (0.004)***		0.012 (0.019)**	0.002 (0.597)
Business Background			0.003 (0.688)	0.004 (0.658)	0.003 (0.654)
Financial Services Background			0.004 (0.336)	0.002 (0.546)	0.006 (0.110)
Prior CEO Experience			-0.009 (0.026)**	-0.008 (0.050)**	-0.006 (0.118)
Prior CFO Experience			0.006 (0.521)	0.008 (0.392)	0.009 (0.237)

In the above models, we consider any variable with a p-value less than 0.10 to be statistically significant, and adopt Model 5 as our primary model due to its comparatively large R-Squared coefficient. Therefore, we conclude that shareholders tended to penalize bank directors for each year of incumbency, for having prior experience in government or the law, and for being an independent of the firm. Conversely, shareholders tended to favor directors who were in charge during the crisis, for serving on the board's nominating committee, and for positive percent changes in stock price. We cannot conclude with statistical confidence that the other independent variables in this model accurately predict shareholder sentiment toward the directors of the firms in this sample. These results are discussed in the following section.

With an overall p-value of zero to four decimal places, the model itself is statistically significant. Approximately 36% of the variability in the proportion of shareholder votes cast in favor of each director is accounted for by the model.

VI. Discussion, Limitations, and Conclusions

Discussion

The hypothesis tests and regressions performed in this study confirm several important features of bank director elections during and after the financial crisis. Primarily, we observe that the directors of bank boards received statistically fewer shareholder votes in favor as a proportion of total votes cast in their annual, or semi-annual, uncontested elections. Meanwhile, Kirkpatrick (2009) establishes that failures in governance on the part of boards of directors of bank holding companies may have triggered, if not caused, the financial crisis. This study's findings, coupled with Kirkpatrick (2009), strongly suggest that shareholders do in fact penalize bank boards for the financial crisis. Notably, however, shareholder disapproval seemed to be stronger after, and not during, the event, which this study defines as occurring in 2007 and 2008. Accordingly, shareholders' attitudes toward directors during times of macroeconomic or industry-wide crisis may not be observable until several years have elapsed. It is also plausible that shareholders may prefer director continuity during times of crisis, but are willing to expel or signal their disapproval of directors once the crisis has largely passed.

Bank shareholders likely took several aforementioned individual, board, and firm-wide factors into account. Notably, however, our model suggests that shareholders penalized independent directors and yet preferred directors who were in charge during the crisis. These seemingly counterintuitive outcomes may be explained by board turnover. It is likely that directors who performed especially poorly in the eyes of shareholders were not renominated or resigned from their boards rather than running for re-election. As a consequence, shareholders may not have been able to formally render a verdict on especially poor directors. Nonetheless, shareholders tended to penalize long-serving directors, which confirms the findings of Schnake, Fredenberge, and Williams (2005). However, if a director was not replaced after the financial crisis, he or she seems to be performing relatively better than new directors.

This study has several important policy implications. In terms of corporate governance policy, it is likely that bank shareholders desire a stronger mechanism to remove poorly performing directors and nominate new people to these important positions. Despite the fact that shareholders disapproved of 76% of bank director-nominees in 2010, only 9% of those directors were not renominated in 2011. The agency problem inherent between shareholders and boards of directors may be mitigated if directors become more vulnerable to shareholder disapproval. Perhaps

shareholders should be permitted to usurp board-nominating committees and put forth director-nominees of their own when directors fail to amass a particular percentage of votes in favor (say, for example, less than 80% or 90%).

Limitations

Data for this study was rather limited, and focused only on director elections from 2006 to 2010, for a total of five distinct years. The effects of the financial crisis have not entirely passed. Further research on this topic may seek to look at years prior to 2006 and after 2010 for a more complete understanding of the financial crisis's effects on bank shareholders, boards, and management. Moreover, this study did not take into account firms that collapsed or merged with other firms. For example, firms like Merrill Lynch, Bear Stearns, and Lehman Brothers were not part of the sample. These exclusions were made in order to ensure uniformity in the data; care was taken to be sure that the data for each firm in the sample could speak to shareholder sentiment before, during, and after the financial crisis. Finally, the OLS regressions used in this study did not include individual or average director compensation, suggesting a possible avenue for future studies on this event. The models and methods offered in this study may also facilitate additional research on the behavior of shareholders and directors of firms within industries suffering from similar pervasive crises, such as the American automotive industry crisis of 2008 to 2010.

Conclusion

This study determined that shareholders of American bank holding companies penalized the members of the firms' boards of directors for the financial crisis during the 2008, 2009, and 2010 board election cycles. However, directors of non-bank holding companies also lost similar levels of shareholder support during the same period of time. Nonetheless, our empirical analysis with data on director elections and characteristics has allowed us to conclude with confidence that shareholders took into account director tenure, experience in government or law, independence from the bank, membership on the firm's nominating committee, and changes in stock price when evaluating directors vis-à-vis director election votes.

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Appendix I: Figures

	Institution Name	Location	Total Assets
1	American Express Company	New York, NY	$152,273,000
2	Associated Banc-Corp	Green Bay, WI	$21,924,217
3	Bank Of America Corporation	Charlotte, NC	$2,136,577,907
4	Bank Of New York Mellon Corporation, The	New York, NY	$325,793,000
5	BB&T Corporation	Winston-Salem, NC	$174,579,294
6	Capital One Financial Corporation	Mclean, VA	$206,103,658
7	CIT Group Inc.	Livingston, NJ	$45,235,752
8	Citigroup Inc.	New York, NY	$1,873,878,000
9	City National Corporation	Los Angeles, CA	$23,666,291
10	Comerica Incorporated	Dallas, TX	$61,139,192
11	Commerce Bancshares, Inc.	Kansas City, MO	$20,663,043
12	Discover Financial Services	Riverwoods, IL	$69,483,014
13	East West Bancorp, Inc.	Pasadena, CA	$21,968,902
14	Fifth Third Bancorp	Cincinnati, OH	$116,966,697
15	First Horizon National Corporation	Memphis, TN	$24,790,132
16	First Niagara Financial Group, Inc.	Buffalo, NY	$32,827,411
17	Goldman Sachs Group, Inc., The	New York, NY	$923,718,000
18	Hancock Holding Company	Gulfport, MS	$19,786,771
19	Huntington Bancshares Incorporated	Columbus, OH	$54,450,652
20	JPMorgan Chase & Co.	New York, NY	$2,265,792,000
21	Keycorp	Cleveland, OH	$88,762,571
22	M&T Bank Corporation	Buffalo, NY	$77,924,287
23	Metlife, Inc.	New York, NY	$799,625,102
24	Morgan Stanley	New York, NY	$749,898,000
25	New York Community Bancorp, Inc.	Westbury, NY	$42,026,245
26	Northern Trust Corporation	Chicago, IL	$100,223,739
27	PNC Financial Services Group, Inc., The	Pittsburgh, PA	$271,407,158
28	Regions Financial Corporation	Birmingham, AL	$127,049,907
29	State Street Corporation	Boston, MA	$216,435,818
30	Suntrust Banks, Inc.	Atlanta, GA	$176,900,103
31	SVB Financial Group	Santa Clara, CA	$19,976,168
32	Synovus Financial Corp.	Columbus, GA	$27,162,845
33	TCF Financial	Wayzata, MI	$18,979,388
34	U.S. Bancorp	Minneapolis, MN	$340,122,000
35	Wells Fargo & Company	San Francisco, CA	$1,313,867,000
36	Zions Bancorporation	Salt Lake City, UT	$53,150,649
		TOTAL	**$12,995,127,913**

Figure 1: Sample of the Top Public American Bank Holding Companies
Source: National Information Center, Federal Reserve System

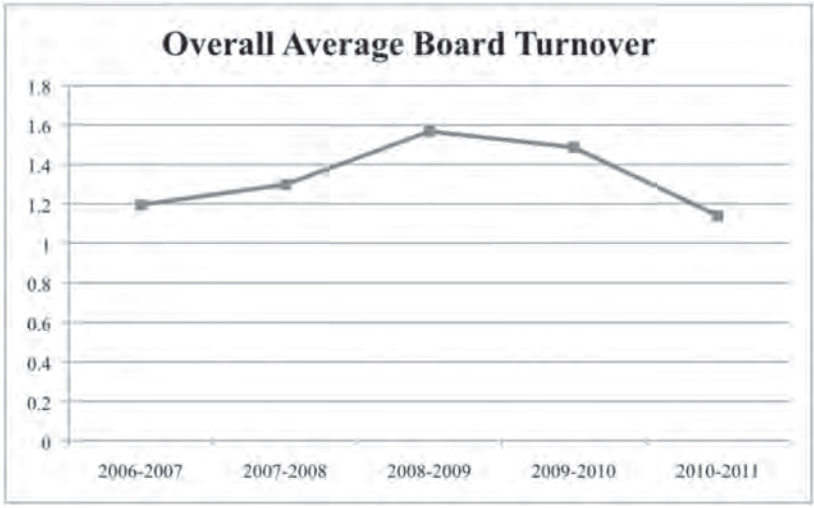

Figure 2: Overall Average Board Turnover
Source: Electronic Data-Gathering, Analysis, and Retrieval System (EDGAR), U.S. Securities and Exchange Commission

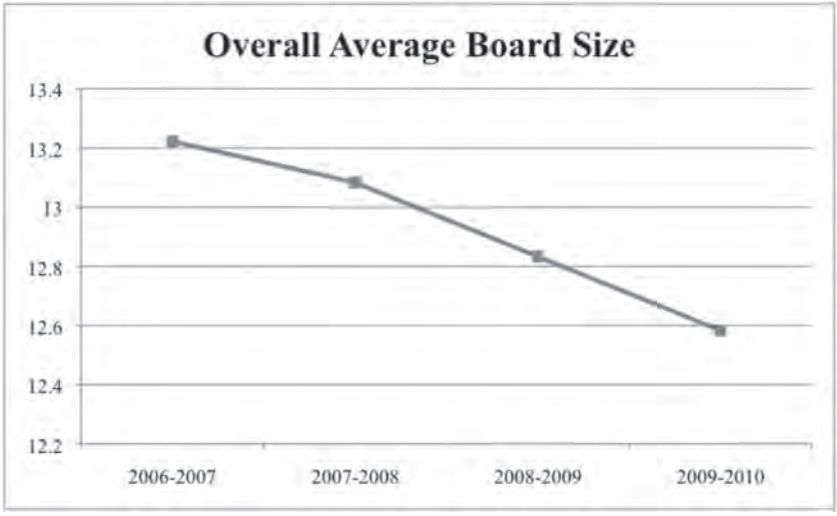

Figure 3: Overall Average Board Size
Source: Electronic Data-Gathering, Analysis, and Retrieval System (EDGAR), U.S. Securities and Exchange Commission

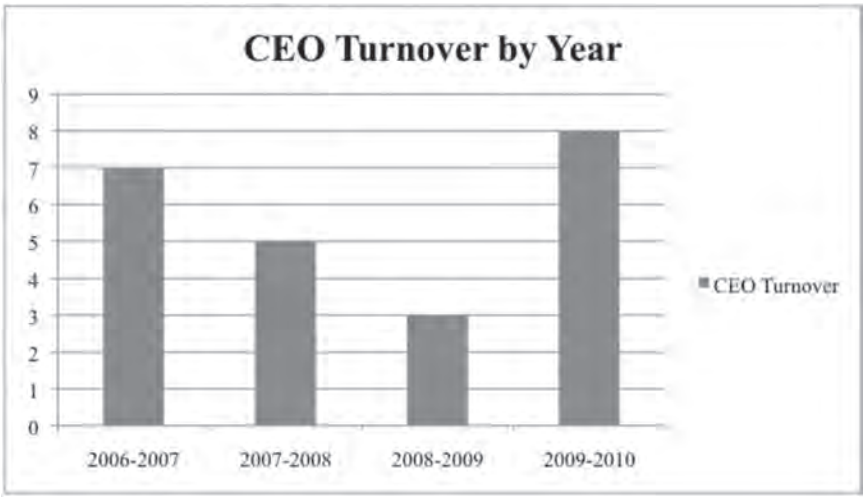

Figure 4: CEO Turnover by Year
Source: Electronic Data-Gathering, Analysis, and Retrieval System (EDGAR), U.S. Securities and Exchange Commission

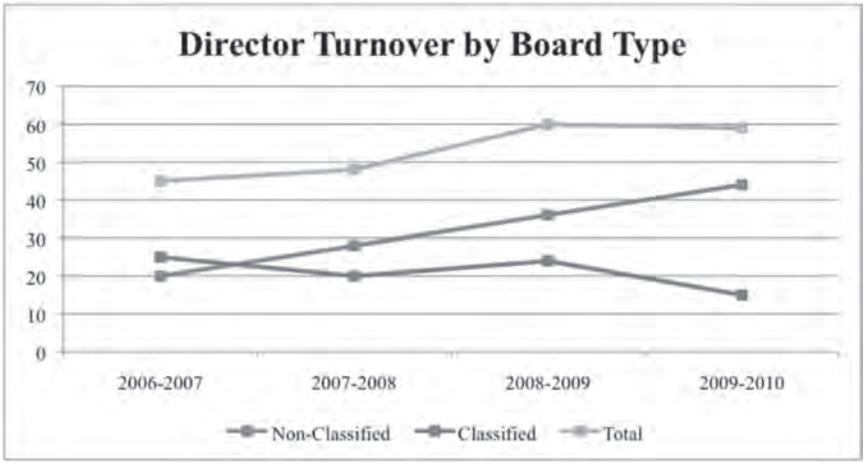

Figure 5: Director Turnover by Board Type
Source: Electronic Data-Gathering, Analysis, and Retrieval System (EDGAR), U.S. Securities and Exchange Commission, and Institutional Shareholder Services

Figure 6: Stock Price vs. Board Changes
Note: Data points are averages across this study's sample of 36 firms.

Source: Electronic Data-Gathering, Analysis, and Retrieval System (EDGAR), U.S. Securities and Exchange Commission, and Institutional Shareholder Services

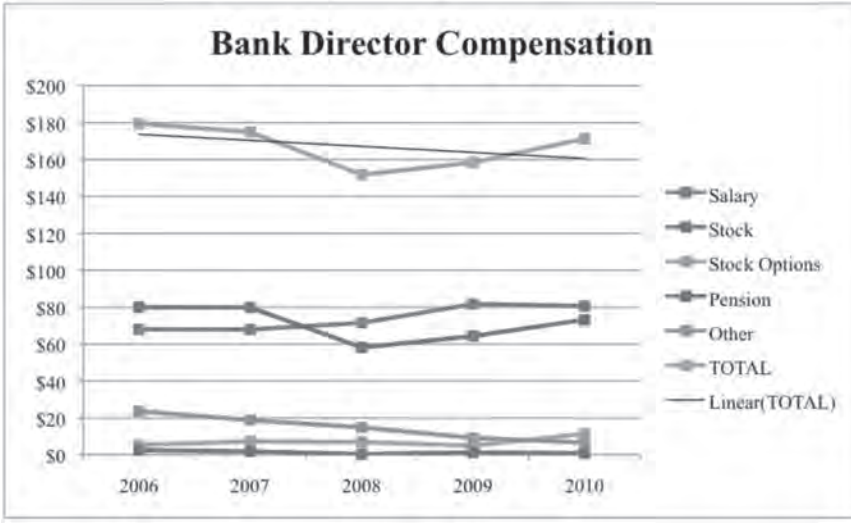

Figure 7: Bank Director Compensation
Source: Wharton Research Data Services (WRDS)

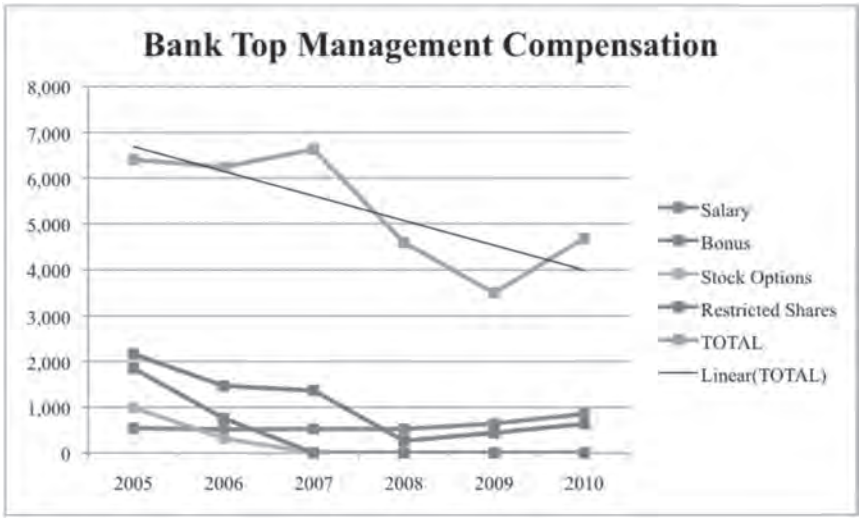

Figure 8: Bank Top Management Compensation
Source: Wharton Research Data Services (WRDS)

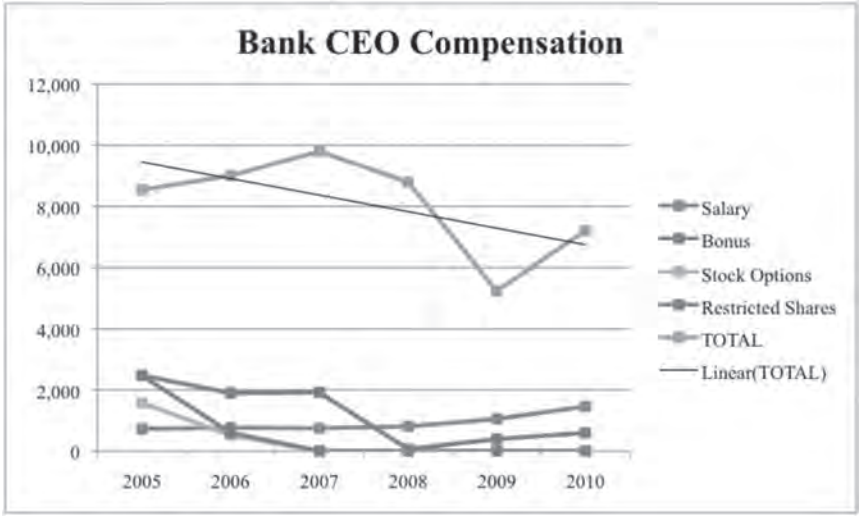

Figure 9: Bank CEO Compensation
Source: Wharton Research Data Services (WRDS)

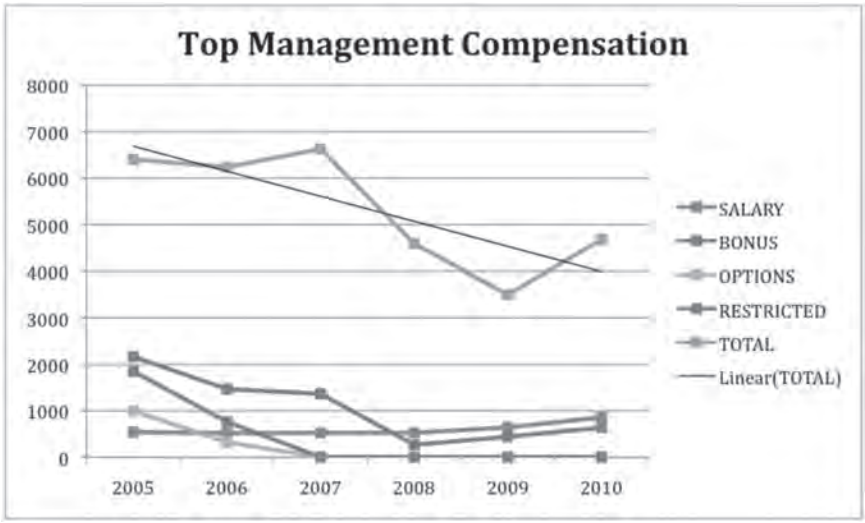

Figure 10: Top Management Compensation

Appendix II: Variable Definitions

%Δ in Current Stock Price is the difference between the opening stock price on the date of the current year's shareholder proxy meeting and the opening stock price on the date of the previous year's shareholder proxy meeting, divided by the previous year's opening stock price.

Academic Background is a dummy variable where 1 indicates that the director nominee has served in a full-time academic role at, for example, a university or think tank; and/or has obtained a Ph.D. or other advanced academic degree.

Audit Committee is a dummy variable where 1 indicates that the director-nominee is currently a member of that firm's audit committee, a committee of the board that is generally responsible for ensuring that the firm's financial statements are accurate.

Board Tenure is the number of years the director has served on this board. It also includes non-consecutive years served.

Business Background is a dummy variable where 1 indicates that the director-nominee has previously worked for a for-profit institution.

Classified Board is a dummy variable where 1 indicates that members of the firm's board are divided into three groups, or "classes," each of which serves three-year terms before needing to be renominated.

Compensation Committee is a dummy variable where 1 indicates that the director-nominee is currently a member of that firm's compensation committee, a committee of the board which is generally responsible for determining the compensation packages of top management and members of the board.

Director During Crisis is a dummy variable where 1 indicates that the director was on the bank's board during the financial crisis of 2007 and 2008.

Financial Services Background is a dummy variable where 1 indicates that the director-nominee has previously worked for a for-profit institution in the financial services industry.

Government Background is a dummy variable where 1 indicates that the director-nominee has previously served in the public sector, including the Federal Reserve System or elected office.

Independent Director is a dummy variable where 1 indicates that the director-nominee is independent of firm management, as per SEC laws.

Legal Background is a dummy variable where 1 indicates that the director-nominee has obtained a Juris Doctor degree and/or has worked in the legal field.

Nominating Committee is a dummy variable where 1 indicates that the director-nominee is currently a member of that firm's nominating committee, a committee of the board that is generally responsible for submitting director-nominees to shareholders each year.

Number of Other Directorships is the number of other boards that a director-nominee has previously served on or is currently serving on at the time of his or her nomination to the bank's board.

Prior CEO Experience is a dummy variable where 1 indicates that the director-nominee has served as the chief executive officer of a firm.

Prior CFO Experience is a dummy variable where 1 indicates that the director-nominee has served as the chief financial officer of a firm.

Prior Director Experience is a dummy variable where 1 indicates that the director-nominee has previously served as a member of the board of directors of another firm at some point in his or her career.

Vote For Percentage is the average percent of "for" votes of all directors being elected in a company. It is calculated by dividing the number of "for" votes for each director divided by the total number of votes cast in that director election.