Do Bank Boards Focus Adequately On Risk?*

Samanvaya Agarwal Saipriya Kamath
Krishnamurthy Subramanian Prasanna Tantri

November 2015

Prior academic research on bank risk-taking has mostly concentrated on the role of board *structure*. However, board *conduct* and its relationship to risk-taking by banks has not received much attention. In this paper, we fill this gap by analyzing the minutes of board and risk management committee (RMC) meetings of 29 banks. We manually classify the issues into different categories, and code whether each issue has been deliberated at length. Among the issues tabled, risk accounts for only 11% while regulation and compliance account for the most (37%) followed by business strategy (35%). Only 20% of the issues are deliberated at length. The RMC meets infrequently and deliberates only 28% of the issues. Only 25% of the issues tabled in the RMC are forward-looking in nature. We interpret this evidence to imply that bank boards focus inadequately on risk and adopt a "box ticking" approach instead of focusing in spirit on risk oversight.

Key Words: Banks, Bank Failure, Board of directors, Board minutes, Corporate governance, Risk, Risk-taking

JEL Classification: G30, L20

Please address correspondence to:
Krishnamurthy Subramanian, Indian School of Business, Gachibowli, Hyderabad, 500032, India. Email: Krishnamurthy_Subramanian@isb.edu

*All the authors are from Indian School of Business, Hyderabad, India. This research is supported by the National Stock Exchange (NSE) - Indira Gandhi Development Institute For Economic Research (IGIDR). The usual disclaimer applies.

I Introduction

The global financial crisis called into question the role of the board in curbing risk-taking in banks. Several reports have highlighted that excessive risk-taking in banks stemmed from the failure of board of directors in appreciating the risks taken by their banks and the related lack of challenge within the boardroom.[1] For instance, the UNCTAD report on "Corporate governance in the wake of the financial crisis" mentions as a key message: "...reform efforts (in financial institutions) should focus on positioning risk management as a key board responsibility." Walker (2009) mentions that "board-level engagement in risk oversight should be materially increased, with particular attention to the monitoring of risk and discussion leading to decisions on the entity's risk appetite and tolerance."

Failure of risk management by bank boards can occur when board members lack the expertise or the incentives to understand the bank's risk (Mehran, Morrison, and Shapiro (2011)). Failure can also occur when risk related topics do not get sufficient attention in board meetings, either due to members of the board not allocating enough time to risk oversight or because matters relating to regulation and compliance consume a significant portion of board time. Prior academic research has mostly concentrated on how board *structure* affects bank risk-taking (see Mehran, Morrison, and Shapiro (2011) for a comprehensive review). However, board *conduct* and its relationship to risk-taking by banks has not received much attention. In this paper, we attempt to fill this gap by examining if bank boards and their committees focus adequately on risk. We use a unique dataset comprised of minutes of board meetings and board-level committee meetings of 29 Indian banks to study this important question.

Compared to American firms, where the minutes are subject to scrutiny by legal experts (Schwartz-Ziv and Weisbach (2013)), these minutes are significantly more detailed. Moreover, the minutes clearly identify the statements/arguments made by individual directors. We transform the minutes into a quantitative database, which enables us to draw inferences about the quality and quantity of discussions relating to the various functions in a bank. We classify the issues that are tabled in these meetings into five categories: risk, business strategy, financial reporting, regulation and compliance, and human resources. For each issue, we record the category to which the issue belongs and whether the board deliberated at length on the issue or not. We record an issue as having been deliberated if the board (i) asked for more information, (ii) elaborately discussed the issue, and/or (iii) the board rejected a proposal or modified it. We also use text analysis methodology suggested by Muslu, Radhakrishnan, Subramanyam, and Lim (2014) to analyze whether an issue is forward looking or not.

[1]For a select few, see Senior Supervisors Group (2014); Walker (2009); UNCTAD (2010); Sheifer (2011); Group (2012)

Methodologically, an analysis of board and board-level committee meeting minutes provides several advantages. First, while board structure captures *de jure* aspects of the board, board minutes capture the *de facto* working of the board. Second, board minutes enables us to understand the complexity and nuanced details of the topics brought up in the board and board-level committee meetings. Third, because banks are highly regulated entities, boards may resort to "box ticking" to comply with regulations and not emphasise analysis of risk in its spirit. Examining the minutes enables us to draw these distinctions. Finally, and most importantly, analysis of the minutes allows us to assess the quality of discussions in the board and board-level committees.

We find that the average number of issues brought forth before a bank board is 50 as compared to the 8.5 in boards of industrial firms as shown in Schwartz-Ziv and Weisbach (2013). Regulatory and compliance related issues account for the most (37%) of the issues tabled followed by issues relating to business strategy (35%). More importantly, among the issues tabled in boards, issues relating to risk only account for 11% of the total issues. To test if the boards just resort to "box ticking" or deliberate on the issues at length, we examine the proportion of issues deliberated. On average, only 20% of the issues that are tabled are deliberated at length.

A natural question to ask would be whether boards are discussing risk in the board-level committees. We examine the minutes of risk management committee (RMC) meetings to understand the quality of risk discussions. On average, RMC meets only a third of the times the board meets and deliberates at length only on 28% of the issues tabled. The RMC spends a larger portion of its time receiving updates and reports than ratifying decisions. Finally, only 25% of the issues tabled in the RMC are forward-looking in nature.

Collectively, these findings provide important insights into the conduct of bank boards. Although no theoretical model predicts the optimal level of attention that a bank board should pay to various issues, we allude to the multi-tasking model by Holmstrom and Milgrom (1991) to interpret the above results. First, our results suggest that bank boards are not paying adequate attention to matters relating to risk. Walker (2009) mentions that "the overriding strategic objective of a bank/financial institution is the successful management of financial risk." The supervision manual of the Federal Reserve states that "The board of directors is responsible to the bank's depositors, other creditors, and shareholders for safeguarding their interests" (see section 5000.1). Thus, given the multi-tasking in effort by directors to minimize risk, on the one hand, and maximize shareholder value, on the other hand, risk issues should be brought up at least as much as those pertaining to maximization of shareholder value. Because issues relating to business strategy and financial reporting clearly correspond to maximization of shareholder value, the disparity—46% on value maximization versus 11% on risk—suggests inadequate board focus to matters relating to risk. This interpretation is buttressed by the relatively

infrequent meetings of the RMC, the poor levels of deliberation, low proportion of forward looking analysis and low percentage of ratification of decisions in the RMC.

Second, our evidence suggests that merely mandating a RMC is insufficient to ensure adequate risk oversight by the board. The Dodd Frank Act (2010) requires large financial institutions to establish a separate RMC comprised of at least one risk management expert. In India, the Reserve Bank of India has mandated RMC since 2002. Yet, the unflattering evidence about the conduct of RMC highlights the oft repeated notion that "form does not lead to substance!"

Third, bank boards seem to be more concerned with fulfilling their duties as laid down by the regulators in letter than in spirit. Complying with regulatory requirements represents a measurable *outcome*. Moreover, the penalties associated with non-compliance are huge. In contrast, risk oversight represents a *process* that cannot be usually measured (except when failure provides measurable evidence of failure of the process). Again, the Holmstrom and Milgrom (1991) model suggests that effort in measurable activities —regulation and compliance — would crowd out effort in non-measurable activites — the process of risk oversight. Our finding that regulatory and compliance related issues account for the most (37%) of the issues while issues relating to risk only account for 11% of is consistent with this prediction. These findings also lead us to speculate that regulation and compliance may be leading to cognitive overload on bank boards, which thereby may lead to boards adopting a "box ticking" approach to risk oversight.[2]

Finally, we find only five cases of recorded dissent among the board of directors, which suggests high degree of conformism and lack of adequate challenge in bank boards. The Walker Report (2009), which reviews corporate governance in UK banks, mentions that the sequence in board discussion should start with an idea being presented, followed by the idea being challenged. Our evidence of lack of challenge in bank boards is thus consistent with the anecdotal evidence mentioned in this report.

Our study focuses on board and RMC minutes from Indian banks. For several reasons, our findings have wide relevance. First, India is English-speaking and has English legal origin (La Porta, Lopez-de Silanes, Shleifer, and Vishny (1998)). Thus, its legal institutions are similar to those in the U.S. or U.K. Second, as Indian accounting and financial data is generally of good quality, recent studies have used the Indian context to examine various issues in financial intermediation (see Visaria (2009), Lilienfeld-Toal, Mookherjee, and Visaria (2012), Vig (2013), Gopalan, Mukherjee, and Singh (2014), Fisman, Paravisini, and Vig (2012)). Third, as already mentioned, RMC has been mandated in India since 2002. Therefore, any additional benefits for risk oversight provided by an RMC can be examined using the Indian setting.

[2]Directors are frustrated with the amount of time they must spend on regulatory and financial compliance matters time that would be better spent talking about... proactive risk mitigation activities" Ernst&Young (2013).

Finally, and most crucially, the Indian banking sector comprises of both government-owned banks as well as private-sector banks. Our sample of board minutes reflects this reality as well. Government ownership of banks is pervasive across the world (La Porta, Lopez-de Silanes, and Shleifer (2002)). Therefore, given the worldwide concerns about corporate governance in banks, analysis of board conduct must ideally include both private-sector and government-owned banks. However, in contrast to our sample, analyses of board conduct using U.S. or U.K. banks cannot generalize internationally because the comparison between private sector banks and government-owned banks cannot be made within the same jurisdiction.

Conceptually, board conduct in government-owned banks may or may not be different from that in private-sector banks. On the one hand, unlike private sector banks where directors are elected by shareholders, directors in government-owned banks are appointed by the government. Given the political interference in government-owned banks (Khwaja and Mian (2005), Cole (2009b)), boards of government-owned banks may reflect the political realities in a country. As a result, board conduct in private sector banks may be different from that in government-owned banks. On the other hand, given the overbearing nature of regulation and compliance in banks, the incentives to comply with the same may drive out other incentives at the board level. Rajan (2009), for instance, states that "there is little evidence that government ownership creates deep differences in employee actions and behaviour." Also, Cole, Kanz, and Klapper (2015) and Bhaumik, Dang, and Kutan (2011) do not find any difference in the way in which employees of government-owned and private-sector banks respond to incentives. Thus, board conduct in government-owned banks may not be substantially different from that in private-sector banks. Our evidence supports the latter hypothesis as we find no differences between government-owned banks and private-sector banks with respect to risk oversight by their boards.

To our knowledge, ours is the first study to examine the conduct of bank boards. Our study thus complements research that focuses on how the structure of bank boards — board size, board independence, and characteristics of the board members including their financial expertise — affects bank risk-taking (see Mehran et al., 2011 and the studies cited therein). Our work also relates to the literature examining risk-management in banks (Ellul and Yerramilli (2013), Aebi, Sabato, and Schmid (2012), Mongiardino and Plath (2010)). Our study closely resembles Schwartz-Ziv and Weisbach (2013), who examine board conduct in non-financial firms and relate their evidence to various theories by carefully analysing board minutes of Israeli government-controlled companies.

II Fiduciary Responsibilities of Bank Boards

Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment (Shleifer and Vishny

(1997). In the corporate governance setting, board of directors provides a mechanism to mitigate conflict of interest between managers and shareholders. In non-financial firms, it is generally accepted that board of directors owe fiduciary duties towards shareholders while bondholders have other mechanisms such as covenants to protect their interests. However, corporate governance in banks is much more complex due to the relevance of banks in the economic system and the nature of banking business (Adams (2010))

Three key differences distinguish the governance of banks from that of industrial firms. First, the capital structure of banks differs substantially from that of industrial firms. Second, partly because of the unique capital structure of banks, but also for other reasons, banks have many more stakeholders than industrial firms (Macey and O'hara (2003), Adams and Mehran (2003)). Finally, banks' business is opaque and complex. Moreover, risks in a bank can change rapidly (Levine (2004)) .

Banks consist of almost 90 percent debt (as opposed to an average of 40% for industrial firms). As well, banks liabilities are largely in the form of deposits, which are available to their creditors/depositors on demand. In contrast, their assets consist primarily of loans that have longer maturities. Despite efforts by banks to loan sales and/or securitization, this mismatch in maturities between the assets and liabilities remains a special attribute of banks. In fact, by holding illiquid assets and issuing liquid liabilities, banks create liquidity in an economy (Macey and O'hara (2003)).

Because of the substantial debt in their capital structure, beyond the shareholders, the stakeholders in a bank include debtholders, the majority of which are the depositors, and the holders of subordinated debt. Apart from the effect of capital structure, there are other important reasons why banks need to care about stakeholders other than the shareholders. In many situations, actions by the shareholders (or the management on behalf of the shareholders) can create spillover effects for other stakeholders (Macey and O'hara (2003)). For example, a failure of a bank can lead to contagion in the banking system and thereby threaten not only the banking system but the macro-economy as well. Inasmuch as a bank's insolvency has negative consequences for the financial system as a whole and these spillovers need to be regulated and/or particular banks need to be bailed out, both at a sizable cost to taxpayers, the government as the regulator becomes a key stakeholder in the bank even when it does not have any ownership in the bank. Of course, when the government is an owner of banks, as it is in the case of government-owned banks, then the government becomes a key stakeholder both as an owner as well as a protector of last resort or an implicit guarantor. The deposit insurance authority also has an interest in the bank's health, as its insurance will be called upon in the case of insolvency. The implementation of deposit insurance poses a regulatory cost of its own — it gives the shareholders and the managers of the insured banks incentives to engage in excessive risk-taking. Such moral hazard—as well as the moral hazard induced by implicit guarantees provided by the government—get exacerbated in situations where a

bank is at or near insolvency (Macey and O'hara (2003)). Furthermore, as depositors are generally small and subject to free-rider issues in monitoring, the importance of other non-equity stakeholders increases (Macey and O'hara (2003)).

Shareholders' interests may diverge substantially from those of other stakeholders, especially on risk, where shareholders prefer volatility and may have short-term perspectives. Clearly, debtholders and regulators prefer low volatility and take longer-term views. Because of the safety net provided by deposit insurance, bank depositors are likely to be less sensitive to bank risk when compared to debtholders in industrial firms. As a result, bank depositors do not demand adequate compensation for risk taking when compared to debtholders in industrial firms. Ceteris paribus, this tendency renders debt a cheap source of funds and biases banks toward it. Regulators could attempt to correct for this bias by charging banks an economic price for their deposit insurance protection as well as any implicit guarantees enjoyed by banks. However, because of the structural opacity of banking assets, reasons for which we describe below, regulators find it very hard to charge banks a fair price for deposit insurance and/or any implicit guarantees.

Banks have the ability to take on risk very quickly and in a way that is not immediately visible to directors or outside investors (Levine (2004)). The risk assumed by banks is quite opaque to directors and outside investors for at least two reasons. First, banks undertake maturity transformation, i.e. invest in risky, illiquid projects using very liquid, 6short-term demand deposits and wholesale funds. As part of this fundamental function that banks perform, banks act as a delegated monitor on behalf of their depositors in selecting and monitoring the projects to which they lend (Diamond and Dybvig (1983)). The literature on banking has emphasized that banks rely significantly on "soft information" for their lending decisions (Berger, Miller, Petersen, Rajan, and Stein (2005), Petersen (2004)). Soft information refers to information that is acquired over time by a loan officer through his/her relationship with the borrower and is therefore hard to communicate to other third parties. Moreover, such information is hard for other third parties to verify as well. As a result, the risks assumed by banks as part of their normal lending business are usually quite difficult for third parties to understand.

Second, banks indulge in technically complex trading activities. The risks assumed by the banks trading divisions are therefore quite difficult for lay investors to comprehend. As Levine (2004) notes, "Banks can alter the risk composition of their assets more quickly than most industrial firms, and banks can readily hide problems by extending loans to clients that cannot service previous debt obligations." Because the risks assumed by banks are not easy for outside investors to assess *a posteriori*, management has the incentive to invest in riskier assets than they promise *a priori* to investors. Because of outside investors inability to assess and monitor the risks assumed by management, oversight over management is delegated to the board as well as regulators.

All the three features—a capital structure dominated by debt, multitude of stakehold-

ers, and opacity and complexity of operations—play a role in governance of banks. These affect the both the interaction between the board and management and the relationship between the bank and its regulators. In fact, because of the special nature of banking and the spillover effects that banks create on other parts of the economy, *the duty of care owed by the board of a bank is substantially more expansive when compared to the duty of care owed by the board of an industrial firm.* In other words, a clear case can be made for bank directors being held to a broader, if not a higher, standard of care than directors in industrial firms. In particular, bank boards owe fiduciary duties to fixed claimants, i.e. the depositors and other debtholders, the regulator as well as to equity claimants.

III Banks in India

As institutional background, we briefly describe the banking system in India and the work of the committee set up by the RBI to review governance of boards of banks in India, on which the present study is based.

III.A Indian Banking System

Banks in India dominate the financial landscape. Flow of funds accounts for the Indian economy show that banking flows account for more than 50% of the total financial flows in the economy.[3] The Indian banking system is divided into following categories: (i) public sector banks, (ii) new private-sector banks, (iii) old private-sector banks, and (iv) foreign banks. Government-owned banks are further divided into the State Bank of India (SBI) and its associates and other government-owned banks. SBI was formed by a separate Act of Parliament soon after India's independence. All other government-owned banks were created by nationalising large private-sector banks in the 1970s and the 1980s. All government-owned banks are listed and hence have significant minority stake. Government stake in government-owned banks varies between 55% and 85%.[4] Smaller private-sector banks, which were not nationalised during the nationalisation spree, continue to operate as old private-sector banks. New private-sector banks were created after India adopted economic liberalisation policy in the year 1991. Finally, foreign banks are fully owned subsidiaries of non-Indian banks, which are registered as foreign banks in India. The entire banking system is regulated by the banking regulator—the Reserve Bank of India (RBI).

Corporate Governance in government-owned banks and privately owned banks differ significantly. The Ministry of Finance, Government of India effectively exercise the powers of a majority shareholder in government-owned banks. Laws that govern government-

[3]Source: http://www.rbi.org.in/scripts/PublicationsView.aspx?id=15440

[4]Source: http://financialservices.gov.in/banking/Shareholding

owned banks lay down rules regarding corporate governance—the SBI Act of 1955 for the State Bank of India and the Nationalisation Acts of 1967 and 1980 for the other government-owned banks. The respective acts applicable to government-owned banks specify the types of directors to be chosen and the way such directors are to be chosen. These different category of directors include representatives of the Government and the RBI, qualified finance professionals, employee representatives. After listing, the respective acts have been amended to include shareholder elected directors on the board. The position of the Chairman of the board and CEO are held by a single individual. As a majority shareholder, the Government gets to appoint the CEO and the same is done through a bureaucratic process.

Private-sector banks, on the other hand, follow the general corporate law with respect to corporate governance. Private bank boards comprise of both executive as well as independent directors in accordance with general corporate law. Private-sector banks follow international best practices in matters pertaining to appointment of the CEO. The process starts with appointment of a search committee comprising of experts in banking and related areas and culminates with shareholder nod for such proposed appointment.

III.B Representativeness

At this stage, it is pertinent to examine how representative are Indian when compared to banks internationally. This question is critical from the point of view of generalisability of our findings. Here, we compare Indian banks with their global peers in terms of some key banking parameters.

III.B.1 Size

It is well accepted that size has implications for the way the bank operates (Berger, Miller, Petersen, Rajan, and Stein (2005). Thus it is important to compare Indian banks with their global peers in terms of size. The total market capitalisation of Indian listed banks is in excess of $205 billion.[5] This is more than 10% of India's GDP and more than 15% of market value of all listed companies in India. As seen in column 2 of table 1, which reports the market capitalisation of Indian banks. Some of the large banks compare well with their global peers in terms of size. HDFC Bank, the largest Indian bank by market capitalisation is ranked 52nd in the world in terms of market capitalisation with a market capitalisation in excess of $32 billion.[6] This compares well with market capitalisation of some of the well known banks in the world such as Deutsche Bank AG of Germany ($45.69 billion), Society Generale of France ($47.62 billion), Credit Suisse group of Switzerland ($51.51 billion) and Standard Chartered Bank of U.K ($51.58 billion). ICICI Bank, the

[5] The market cap is calculated as on December 11, 2014 at the prevailing exchange rate

[6] http://www.relbanks.com/worlds-top-banks/market-cap

second largest private-sector bank by market capitalisation and largest private sector bank by book value of assets, having a market capitalisation in excess of $25 billion, is ranked 66th in the world. The largest public sector bank-State Bank of India is ranked 66th. It is also important to note that three Indian banks are a part of top 100 in the world in terms of market capitalisation. This is comparable to industrial economies such as U.K (5), Canada (5), Japan (4), Australia (4), France (3), Germany (2), and Brazil and South Korea (1 each).

III.B.2 Operational and Financial Performance

Indian banks compare well with their global peers with respect to operational and financial performance. Summary statistics regarding performance of Indian banks is presented in Table 2. Indian banks maintain a capital adequacy ratio of 13.2, which is 65% higher than the Basel II norms. These numbers compare well with the average capital adequacy ratio of 15.46 maintained by American Banks.[7] In terms of operational parameters such as return on assets (ROA), proportion of non-performing assets (NPA), net interest margin (NIM), Indian banks' performance is comparable to global standards. However consistent with the political economy literature (Cole (2009a)), private banks outperform government-owned banks in almost all parameters. Panel B of Table 2 shows that for private-sector banks average ROA is 1.33%, Gross NPA to assets ratio is 1% and NIM is 2.75% . The same numbers for public sector banks turn equal 0.72%, 2.2% and 2.30% respectively.

III.B.3 Regulation

Indian banks are governed by an independent regulator—the RBI. Although the Governor of RBI and his four deputies are appointed by the Government, RBI has developed a reputation as a professional and independent regulator. Successive Governors have resisted pressure from the Ministry of finance with regards to monetary and regulatory policy and used their professional judgments instead (Subbarao (2011)). Especially in the post-liberalization era there is not even a single instance of either government issuing directions to the Central Bank or abruptly removing a RBI Governor for failing to toe the Government's line.[8] It is also important to note that India is a vibrant democracy and any move seen as arbitrary and politically motivated can invite voter's backlash.

Because government ownership of banks is pervasive across the world (La Porta, Lopez-de Silanes, and Shleifer (2002)), the Indian setting provides an apt laboratory to examine the concerns of board conduct in banks worldwide. This is because, unlike banks in the U.S. and U.K., the Indian banking sector includes both private-sector banks and

[7] http://www.newyorkfed.org/research/banking_research/QuarterlyTrends2013Q2.pdf"

[8] Source:http://www.livemint.com/Home-Page/hVTYJEt0JJpLqbSZSCg1uK/How-independent-is-RBI.html

government-owned banks. In contrast to our sample, analyses of board conduct using U.S. or U.K. banks cannot generalize internationally because the comparison between private-sector banks and government-owned banks cannot be made within the same jurisdiction.

III.C RBI Committee on Governance of Bank Boards

In order to review the governance practices in the boards of Indian banks, the RBI constituted an expert committee in January 2014. The committee was headed by Dr. P. J. Nayak, the former managing director and chairman of Axis bank—India's third largest private-sector bank—for over 10 years between 2002 and 2012. The committee consisted of experts from diverse fields such as law, consulting, academia and government. The corresponding author of this paper was a member of and director of research for the committee. The other three authors assisted the committee in its research work.

The terms of reference given to the committee were comprehensive. Among other things, the RBI specifically asked the committee to (i) examine the working of bank boards including whether adequate attention is devoted to issues of strategy, growth, governance and risk management; (ii) analyze the representation on bank boards to see whether the boards have the appropriate mix of capabilities and the necessary independence to govern the institution; and (iii) investigate possible conflicts of interest in board representation, including among owner representatives and regulators. The committee submitted its report to the RBI on 5th of May 2014.

IV Data and Methodology

Our data is based on the minutes of bank board meetings from the RBI committee on governance of bank boards. To fulfill its mandate, the committee requested all major banks in India to provide detailed minutes of their latest board meeting. The request was sent to 24 government-owned banks and 17 privately owned banks. The request was sent during the second week of February 2014. Due to time constraints, the committee collected the minutes pertaining to only one board meeting per bank. Not all banks had completed by then the board meeting for the third quarter. Hence, the committee requested banks to share the minutes for their second quarter meeting. 12 government-owned banks and 9 private banks provided the required data. The banks that provided data account of 70% of market capitalization and 65% of revenues all banks in India.

Representative data from the minutes of a board and board-level committee meeting contain the following information: name of the bank, date and venue of the meeting, names of the directors who attended the meeting, names of the bank executives (other than directors) who were invited to the meeting, agenda for the meeting and the way the agenda items were deliberated and resolved. The document further provides information

about each item on the agenda. A brief explanation is provided about the agenda item. The document then records the views expressed by the members of the board on that agenda item. Finally, the document records the resolution that was passed by the board and the descent (if any) recorded by any individual board member(s). If the board gives any instructions to the management with regards to any kind of follow up actions to be taken, then the same is recorded as a part of the resolution.

The data pertaining to real outcomes such as proportion of non performing assets, return on assets, net interest income etc were obtained from Prowess database maintained by the Center For Monitoring Indian Economy (CMIE). CMIE is a leading Indian policy research organization, which specializes in collection and dissemination of Indian corporate data. A number of prominent studies have used Prowess database provided by CMIE (see Bertrand, Mehta, and Mullainathan (2000), Khanna and Palepu (2000) and Gopalan, Nanda, and Seru (2007)).

IV.A Archival Data vs. Board and Committee Minutes

Since our study is based on the analysis of minutes from the board and committee meetings, we examine the pros and cons of this approach vis-a-vis analysis based on archival data.

First, board composition captures *de jure* aspects of the board. The *de facto* workings of the board can, however, differ substantially because of the interpersonal interactions and the interpersonal relationships between the board members. Such *de facto* workings are more likely to be captured by examining detailed board minutes, which record participation in the deliberations by each member.

Second, variables pertaining to board composition cannot capture qualitative, yet nuanced, aspects of risk-taking. For instance, because any analysis of risk has to be forward-looking, analysis of minutes of the board as well as the risk management committee can reveal the extent to which forward-looking discussions were undertaken by the board or its committees. Such aspects cannot be captured in archival research based on variables relating to board composition.

Third, because banks are highly regulated entities, boards may resort to “box ticking” to comply with regulations and not emphasise analysis of risk in spirit. Again, such aspects cannot be captured using archival research based on variables relating to board composition.

IV.B Methodology

We now describe our empirical methodology. Since the data is qualitative in nature, it is important to describe the methods used to convert the qualitative database into a quantitative one. We use content-analysis methodology as mentioned in Krippendorff

(2012) and Lieblich, Tuval-Mashiach, and Zilber (1998), which specifies the procedures to reduce words of text into fewer content categories. This methodology involves constructing a quantitative database by categorizing or coding different aspects of a qualitative data set. Using this methodology, we manually classified each of the issues brought up in the minutes into five categories. The coding was undertaken in two steps. First, because the coding guidelines required a comprehensive understanding of the content of the meetings, for a small sample of banks that included government-owned and private-sector banks, all the board meeting papers were read manually. The understanding gained from the leading of the content of the board papers was utilised in developing a coding scheme for categorising the various issues. In this step, a distinction was made between agenda notes and the items for discussion. The focus was on analyzing the items tabled and deliberated rather than mere agenda notes. Second, the actual coding of the issues tabled and discussed in the board documents was undertaken based on the coding scheme that was fine-tuned in the first step.

IV.C Categorisation

We classify all the issues tabled in the board meetings into five board categories. The brief description of these categories is as follows:

1. Risk: Risk management plays a critical role in banking business (Ellul and Yerramilli (2013)). Therefore, we analyze matters relating to risk separately. Matters relating to risk include reviewing large forex exposures, fixing ceilings in different areas, adherence to exposure norm and reviewing credit risk management policy fall under risk discussions.

2. Business Strategy: These include forward looking issues relating to business strategy that have long-term consequences for the bank. We consider only those issues that are not mandated by the regulator as issues mandated for tabling under business strategy. Representative examples would be a proposal to enter insurance business by forging a joint venture with a foreign collaborator, initiating a promotional campaign, and approval of large investments.

3. Financial Reporting: These involve regular stock taking of financial results. These issues are generally based on the management's presentation of financial results for the quarter. These include, for example, discussion of quarterly performance, review of growth of deposits and peer-level performance reviews.

4. Regulation and Compliance: Under this category, the first set of issues are generally tabled and discussed in response to either a specific instruction or a general guideline by regulators. A representative issue in this category would be a

discussion on Anti Money Laundering Guidelines issued by the RBI or on meeting the KYC (Know Your Customer) norms issued by the RBI. Second, banks in India are mandated to direct credit to some sectors, which are identified as priority sectors. Government of India as well as RBI, from time to time, announce financial inclusion schemes to be delivered by banks. Any discussion on these issues come under this category. Third, this category includes issues that must receive the formal approval of the board, such as granting the authority to sign a contract or financial reports, nomination of trustee, power of attorney, etc.

5. HUMAN RESOURCES: This includes issues such as appointments and approvals of directors, perks and perquisites for employees, incentive schemes for employees, promotion policies for employees, training and skill development of employees.

Table 2 shows a few examples of each category of issues.

IV.D Tabling vs. Deliberation of Issues

After recording the issues, we distinguish between mere tabling of issues and their deliberation. If an issue is just presented before the board and the related resolution is deemed to be passed without discussion, then we code such an issue as just presented or tabled without it being deliberated.. If tabling of an issued is followed by discussion on the issue then we code such issue as deliberated. Before coding an issue as deliberated, we make sure that a discussion on the issue is found in the minutes. Specifically, we define an issue as deliberated if the board discusses the issue in detail and takes any of the following actions: (i) directs management for further action; (ii) demands more information; (iii) expresses concern over relevant existing processes, data, performance indicators, etc.; (iv) rejects a new policy or proposal. An issue, where the minutes just mentions that the issue was deliberated without providing details of the discussion, is not considered as deliberated.

IV.E Forward vs. Backward looking statements

We classify issues in risk committee minutes as forward looking or not. To do so, we follow the methodology of Muslu et al. (2014). Using criteria from computational linguistics, we develop a comprehensive list of forward looking words found in the risk committee minutes. Our unit of measurement is a sentence. We identify a sentence as forward looking if it contains any of the following phrases: (1) keywords that implies action to be taken in future (e.g. “future”, “next year”); (2) verb conjugations that indicate the future (e.g. “bank plans to monitor”, “bank shall”). These phrases are developed from our reading of randomly selected committee minutes.

V Results and Discussion

V.A Evidence from Board Minutes

V.A.1 Focus on Risk

Table 3 summarizes the total number of issues tabled in a board meeting for each category. We find that the boards discuss issues relating to regulation and compliance the most, which takes up 37% of the total board time. Issues relating to business strategy are next in importance as they occupy 35% of the time. These numbers are not significantly different for government-owned and private-sector banks. In contrast, boards spend very little time in discussing issues pertaining to risk. In government-owned boards, only 9% of the issues tabled correspond to risk related topics, while in private-sector this percentage 14%.

We argue that the level of risk issues being tabled (11%) across all banks is inadequate. Unlike industries such as infrastructure, construction, retail, or services where shareholder value maximization is the sole objective of the firm, banks have a fiduciary responsibility to their depositors as well. As banks are highly levered with depositors having large stakes in them, risk minimization forms an integral part of the responsibility of the board. Banks perform this role of risk transformation by diversifying their investments, pooling risks, screening and monitoring borrowers, and holding capital reserves in case of any unexpected losses. Therefore, boards in banks have to balance the conflicting objectives of shareholder value maximization and risk minimization. Models of multi-tasking (Holmstrom and Milgrom 1991) suggest that when an agent exerts effort in multiple tasks — in this case shareholder value maximization and risk minimization — incentives effort put in the tasks, incentives will decide how the agent will allocate effort between these tasks. Walker (2009) mentions that "the overriding strategic objective of a bank/financial institution is the successful management of financial risk." The supervision manual of the Federal Reserve states that "The board of directors is responsible to the bank's depositors, other creditors, and shareholders for safeguarding their interests" (see section 5000.1). Moreover, although the penalties from losses in shareholder value is immediate, they are not as severe as in the case of losses arising from poor risk management (Mongiardino and Plath 2010). Therefore, we expect that bank boards should spend at least as much time discussing risk related issues as they spent on issues pertaining to shareholder wealth maximization. We classify shareholder maximization activities as sum total of business strategy and financial reporting, HR issues fall under other activities. Panel B of table 3 shows that bank boards spend about 46% of their time in discussing issues pertaining to shareholder value maximization, while they spend only 11% of their time in discussing risk related issues. Thus, we infer that bank boards do not pay sufficient attention to risk related issues.

V.A.2 Quality of Deliberation

The Walker Report (2009), which reviews corporate governance in UK banks, mentions that the sequence in board discussion should start with an idea being presented, followed by the idea being challenged. To check whether the board follows this sequence, we look at the level of pro-activeness shown by the directors. To this end, we look at whether any board member participates beyond merely giving approval or agreement. Actions such as seeking further information or update, expressing concern, modifying a proposal, and dissenting with the management qualify as identifiers of pro-activeness (issue deliberated).

Table 4 shows the number issues that were deliberated in detail. Columns (1), (4), and (7) display the number of issues that are deliberated in government-owned banks, private-sector banks and all banks respectively. Columns (2), (5), and (8) display issues deliberated as a percentage of the number of issues tabled. Columns (3), (6), and (9) display the fraction of issues deliberated in a category out of all the issues deliberated. Column (8) of table 4 shows that on average, among all banks, a low percentage of issues is deliberated in detail. Among the various categories, we find that percentage of issues deliberated ranges from 14% for regulation and compliance to 23% for financial reporting issues. We also do not find any significant difference in the level of deliberation between private and government-owned banks in most categories except in HR, where government-owned banks deliberate on 27% of HR issues while private-sector banks deliberate on 8% of the HR issues. Overall, our results support the findings in the Walker Report (2009), which identifies lack of ideas being challenged in the board room as one of the principal deficiencies in bank boards.

V.A.3 Deliberation of Issues Relating to Risk

We find that risk issues are deliberated inadequately. Only 15.1% of the risk issues that are tabled are deliberated in detail. Considering that issues relating to risk are more complex in nature, we should expect a higher level of discussion from the board of directors on risk related issues. We also find that of all the issues deliberated across categories, risk takes up only 9.6% of the time.

One explanation for such low levels of tabling and deliberation of risk can be the difficulty in measuring risk. Activities falling under categories such as performance or compliance are easily measurable whereas the only measurable component of risk is whether banks meet various thresholds set by the regulator. Risks assumed by banks are quite opaque for two reasons. First, as part of their fundamental functionality, banks lend money and act as delegated monitors on behalf of their depositors (Diamond and Dybvig (1983)). The literature on banking has emphasized that banks rely on soft information for their lending decisions (Petersen (2004), Berger, Miller, Petersen, Rajan, and Stein

(2005)). Soft information by its very nature is unverifiable (Petersen (2004)). As a result, as part of their normal lending business, the risks that banks assume are opaque and complex. Second, banks indulge in technically complex trading activities, which make it quite difficult for lay investors to comprehend.

Because risks in a bank are not easy to comprehend for the outside investors and depositors, and such risks can change rapidly, the process of risk oversight becomes critical in a bank. However, the process of risk oversight is not easy to measure. Moreover, in a principal agent setting, the adequacy of this process of risk oversight undertaken by the agent is not easy for the principal or for a third party to verify. Because the process of risk oversight is difficult to verify, it is difficult for the principal to design incentives to motivate the agent to undertake risk oversight in its true spirit. This challenge becomes particularly acute when the agent exerts effort in multiple tasks with one of the tasks generating measurable and verifiable output ad the other task generating non-measurable and thereby unverifiable output. As Holmstrom and Milgrom (1991) argue, in such a setting, the effort exerted towards the verifiable setting would crowd out effort exerted towards the non-verifiable outcome. Thus, in our setting, the board of directors would over-invest board time in regulation and compliance activities, which generate verifiable outcomes, at the cost of the process of risk oversight, which is difficult to measure and verify. This might explain why board of directors do not pay as much attention to risk management activities as required.

V.B Evidence from Risk Management Committee Minutes

A natural follow up question that arises is whether banks are discussing risks in any other board-level committee meetings. Indian banks are mandated to constitute a separate risk management committee where these issues could possibly be discussed in detail. This committee is endowed with the responsibility of evaluating overall risks faced by the bank and determining the level of risks, which will be in the best interest of the bank. In the wake of Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, which requires large bank holding companies to create a stand-alone board-level risk committee, it becomes important to understand the kind of discussions that take place in a risk management committee meeting.

Table 5 presents the details of the constitution and the number of meetings of risk management committee as a proportion of the number of times the board of a bank meets. We find that on average, the risk management committee meets only 4 times year, as compared to the 12 annual meetings of the board, or the 10 annual meetings of audit committee. Column 3 of Table 6 shows that in several banks the frequency of RMC meetings are significantly lower than the frequency of board meetings. While frequent meetings are by no means sufficient for robust risk governance, infrequent meetings imply

that the board has insufficient time to review and discuss risk issues. Table 6 shows the kind of issues that are brought up in the risk management committee meetings. Considering the complexity of issues relating to risk that are discussed in these meetings, the frequency of meetings of risk committee may be insufficient.

"They [risk-committee member] need to be aggressive about asking for data. They need to keep asking 'Why?"' - Bert Otto, US Department of Treasury. This quote tells us that a good risk-committee would question policies relating to risk. Thus, risk committee members must be proactive in discussing the issues. As before, we measure pro-activeness by the amount of detailed deliberations taken up during the meeting. Panel A of Table 7 shows that the average number of issues brought up in the risk management committee of a bank is 26, which is quite a large number for a single meeting. Not surprisingly, we find that only 28% of the issues which are tabled are deliberated in detail. This finding supports the view that the risk management committee seems to be indulging in box-ticking for regulatory purposes rather than performing risk assessment, and risk management in their true spirit. Our findings are supported by the findings in Walker Report (2009), which mentions that boards have delegated key parts of risk oversight to the financial compliance function with the object of meeting regulatory capital requirements at minimum cost and with minimum erosion of returns on equity.

We next look at the ratification and monitoring of issues in the risk committee meetings. Ratification and monitoring is defined as in Fama and Jensen (1983). Panel B of table 7 shows the number of issues which are ratified and monitored. Of the total number of issues that are tabled, 73.22% of issues relate to monitoring and the rest are for ratification. Of the deliberated issues, 72.90% pertain to monitoring. Largely, risk committees seem to be performing a monitoring role where they are presented with updates and reports.

Finally, we look at whether the activities of risk-committee are forward looking or backward-looking. The Walker Report (2009) emphasizes the necessity of risk committees to be forward-looking: "Alongside assurance of best practice in the management and control of known and reasonably measurable risks, the key priority is to give clear, explicit and dedicated focus to current and forward-looking aspects of risk exposure". To test whether risk committees are forward looking, we perform text analysis on the minutes of RMC meetings. We operationalise the methodology used in Muslu et al. (2014) using text analytic tools in R. We find that, on average, only 25% of risk committee discussions are forward looking. In this aspect private-sector banks are better than government-owned banks. Private banks discuss forward-looking risks 43% of the time while public banks discuss forward-looking risks only 21% of the time.

Combining the findings that risk committees meet infrequently (4 annually), conduct detailed deliberations only 28% of the time, mostly perform monitoring activities(72%), and discuss forward looking aspects of risk exposure infrequently (25%), we infer that

board-level risk committees also do not discuss risk adequately.

To assess the validity of our measures, we use a bank, which has won multiple awards in the last decade for having the best risk management practices as a benchmark. The RMC of this bank meets 7 times a year, as opposed to the average of 4. In this bank, the percentage of risk issues tabled equals 22%, which is much higher than the average of 11%. The risk committee of this bank ratifies 67% of the issues put forth, while the average is only 26%. The fact that the bank that has been rated as having excellent risk management practices also rates highly on our measures for focus on risk lends credence to our findings.

VI Conclusion

Prior academic research on bank risk-taking has mostly concentrated on the role of board structure. However, board conduct and its relationship to risk-taking by banks has not received much attention. In this paper, we fill this gap by analyzing the minutes of board and risk management committee (RMC) meetings of 29 banks. We manually classify the issues into different categories, and code whether each issue has been deliberated at length. Risk accounts for only 11% of the times with regulation and compliance accounting for the most (37%) followed by business strategy (35%). Only 20% of the issues are deliberated at length. The RMC meets infrequently and deliberates only 28% of the issues. Only 25% of the issues tabled in the RMC are forward-looking in nature. We interpret this evidence to imply that bank boards focus inadequately on risk and adopt a "box ticking" approach instead of focusing in spirit on risk oversight.

Our results have broader relevance than studies that focus on banks in the U.S. or U.K. This is because government ownership of banks is pervasive across the world (La Porta, Lopez-de Silanes, and Shleifer (2002)). Moreover, given the worldwide concerns about corporate governance in banks, analysis of board conduct must include both private-sector and government-owned banks. Unlike banking sectors in U.S. or U.K., where governments invested in distressed banks for a short period following the financial crisis, the Indian banking sector comprises of both government-owned banks as well as private-sector banks. Our sample of board minutes reflects this reality as well. Our finding that neither the boards of government-owned nor those of private-sector banks focus adequately on risk, therefore, raises concerns for policymakers across the world. In particular, policy makers should be concerned about the possibility that regulation and compliance may be leading to cognitive overload on bank boards, which thereby may lead to boards adopting a "box ticking" approach to risk oversight.

We do not imply that compliance occupying more than one third of the board agenda is necessarily a bad outcome. We do recognize that in a pro-active and forward looking regulatory environment, compliance with regulations itself may take care of substantial

part of risk management. However, as we point out in the Introduction, more than two third of compliance related issues are not at all deliberated. Most issues are just presented and approved. Such an approach is unlikely to be optimal even in a good regulatory environment. If the board does not deliberate and examine compliance in detail, the management may get away with window dressing and in spirit violations. However, at some level, we are agnostic to the desirability of the focus on compliance as we cannot distinguish between good and bad regulatory regime. The limited purpose here is to describe the functioning of a typical bank board. We leave it to future research to comment on optimal allocation of bank board time and how the same should vary with the quality of regulation.

We recognize a significant limitation of our study: our sample is restricted to the minutes of one board meeting and one board-level committee meeting for each bank. We hope that subsequent work would overcome this limitation. We hope that our work would motivate follow-up work examining the conduct of bank boards. Subsequent work that throws light on the responsibilities and tasks of the various committees of bank boards would serve to enhance our understanding of the conduct of bank boards.

References

Adams, R., and H. Mehran (2003): "Is corporate governance different for bank holding companies?," *Economic Policy Review*, (Apr), 123–142.

Adams, R. B. (2010): "Asking directors about their dual roles," in *Finance and Corporate Governance Conference*.

Aebi, V., G. Sabato, and M. Schmid (2012): "Risk management, corporate governance, and bank performance in the financial crisis," *Journal of Banking & Finance*, 36(12), 3213–3226.

Berger, A. N., N. H. Miller, M. A. Petersen, R. G. Rajan, and J. C. Stein (2005): "Does function follow organizational form? Evidence from the lending practices of large and small banks," *Journal of Financial economics*, 76(2), 237–269.

Bertrand, M., P. Mehta, and S. Mullainathan (2000): "Ferreting out tunneling: An application to Indian business groups," Discussion paper, National Bureau of Economic Research.

Bhaumik, S. K., V. Dang, and A. M. Kutan (2011): "Implications of bank ownership for the credit channel of monetary policy transmission: Evidence from India," *Journal of Banking & Finance*, 35(9), 2418–2428.

Cole, S. (2009a): "Financial development, bank ownership, and growth: or, does quantity imply quality?," *The Review of Economics and Statistics*, 91(1), 33–51.

——— (2009b): "Fixing market failures or fixing elections? Agricultural credit in India," *American Economic Journal: Applied Economics*, pp. 219–250.

Cole, S., M. Kanz, and L. Klapper (2015): "Incentivizing Calculated Risk-Taking: Evidence from an Experiment with Commercial Bank Loan Officers," *The Journal of Finance*, 70(2), 537–575.

Diamond, D. W., and P. H. Dybvig (1983): "Bank runs, deposit insurance, and liquidity," *The journal of political economy*, pp. 401–419.

Ellul, A., and V. Yerramilli (2013): "Stronger risk controls, lower risk: Evidence from US bank holding companies," *The Journal of Finance*, 68(5), 1757–1803.

Ernst&Young (2013): "The critical role of the board in effective risk oversight," .

Fisman, R., D. Paravisini, and V. Vig (2012): "Cultural proximity and loan outcomes," Discussion paper, National Bureau of Economic Research.

Gopalan, R., A. Mukherjee, and M. Singh (2014): "Do Debt Contract Enforcement Costs Affect Financing and Asset Structure?," *Available at SSRN 2186835.*

Gopalan, R., V. Nanda, and A. Seru (2007): "Affiliated firms and financial support: Evidence from Indian business groups," *Journal of Financial Economics*, 86(3), 759–795.

Group, G. W. (2012): "Toward Effective Governance of Financial Institutions," *Washington, DC.*

Holmstrom, B., and P. Milgrom (1991): "Multitask Principal-Agent Analyses: Incentive Contracts, Asset Ownership, and Job Design," *Journal of Law, Economics, & Organization*, 7, 24–52.

Khanna, T., and K. Palepu (2000): "Is group affiliation profitable in emerging markets? An analysis of diversified Indian business groups," *The Journal of Finance*, 55(2), 867–891.

Khwaja, A. I., and A. Mian (2005): "Do lenders favor politically connected firms? Rent provision in an emerging financial market," *The Quarterly Journal of Economics*, pp. 1371–1411.

Krippendorff, K. (2012): *Content analysis: An introduction to its methodology.* Sage.

La Porta, R., F. Lopez-de Silanes, and A. Shleifer (2002): "Government ownership of banks," *The Journal of Finance*, 57(1), 265–301.

La Porta, R., F. Lopez-de Silanes, A. Shleifer, and R. W. Vishny (1998): "Law and Finance," *The Journal of Political Economy*, 106(6), 1113–1155.

Levine, R. (2004): *The corporate governance of banks: A concise discussion of concepts and evidence*, vol. 3404. World Bank Publications.

Lieblich, A., R. Tuval-Mashiach, and T. Zilber (1998): "Narrative research," *Reading, analysis and interpretation*, 47.

Lilienfeld-Toal, U. v., D. Mookherjee, and S. Visaria (2012): "The Distributive Impact of Reforms in Credit Enforcement: Evidence From Indian Debt Recovery Tribunals," *Econometrica*, 80(2), 497–558.

Macey, J. R., and M. O'hara (2003): "The corporate governance of banks," *Economic Policy Review*, 9(1).

Mehran, H., A. D. Morrison, and J. D. Shapiro (2011): "Corporate governance and banks: What have we learned from the financial crisis?," *FRB of New York Staff Report*, (502).

Mongiardino, A., and C. Plath (2010): "Risk governance at large banks : have any lessons been learned?," *Journal of risk management in financial institutions*, 3.2009/10(2), 116–123.

Muslu, V., S. Radhakrishnan, K. R. Subramanyam, and D. Lim (2014): "Forward-Looking MD&A Disclosures and the Information Environment," *Management Science*, 61(5), 931–48.

Petersen, M. A. (2004): "Information: Hard and soft," Discussion paper, working paper, Northwestern University.

Rajan, R. G. (2009): "A hundred small steps: report of the committee on financial sector reforms," .

Schwartz-Ziv, M., and M. S. Weisbach (2013): "What do boards really do? Evidence from minutes of board meetings," *Journal of Financial Economics*, 108(2), 349–366.

Senior Supervisors Group (2014): "For more information, see http://www.newyorkfed.org/newsevents/news/banking2014/SSG_Progress_Report_on_Counterparty_January2014.pdf," Discussion paper, Senior Supervisors Group.

Sheifer, A. (2011): "Transformation of Finance," .

Shleifer, A., and R. W. Vishny (1997): "A survey of corporate governance," *The journal of finance*, 52(2), 737–783.

Subbarao, D. (2011): "Central bank governance issues: some RBI perspectives," in *comments at the meeting of the Central Bank Governance Group in Basel on*, vol. 9.

UNCTAD (2010): "Corporate Governance in the wake of the financial crisis," Discussion paper.

Vig, V. (2013): "Access to Collateral and Corporate Debt Structure: Evidence from a Natural Experiment," *Journal of Finance*, 68(3), 881–928.

Visaria, S. (2009): "Legal Reform and Loan Repayment: The Microeconomic Impact of Debt Recovery Tribunals in India," *American Economic Journal: Applied Economics*, 1(3), 59–81.

Walker, D. (2009): "A review of corporate governance in UK banks and other financial industry entities," Discussion paper.

Table 1: Summary Statistics For Indian Banks

This table reports summary statistics pertaining to operating performance, ownership and market capitalisation of Indian banks. The Market Capitalisation is calculated based on closing share price as on 31st March-2014. Government ownership is also calculated as on 31st March 2014. Other operating metrics are averaged over 2005-06 to 2013-2014. CAR refers to Capital Adequacy Ratio, NIM stands for Net Interest Margin, NII refers to Net Interest Income, NPA refers to Non Performing Assets, ROA refers to Return on Assets and finally P/B ratio refers to Profit to Book Ratio.

Panel A: Government-Owned Banks

Bank	Market Cap (In Rs. Billion)	CAR	NIM	NII Growth	Net NPA	ROA	P/B ratio	Profit Growth	Govt Stake
Allahabad Bank	49.5	12.662	2.525	0.185	1.148	1.129	1.024	0.144	0.55
Andhra Bank	37.7	12.836	2.758	0.181	0.548	1.273	1.177	0.151	0.580
Bank of Baroda	309.5	13.544	2.428	0.188	0.690	1.000	1.148	0.276	0.550
Bank of India	146.7	11.906	2.265	0.196	1.328	0.841	1.253	0.383	0.640
Bank of Maharashtra	33.2	12.229	2.535	0.176	1.263	0.599	0.872	0.623	0.810
Canara Bank	121.9	13.313	2.275	0.132	1.297	1.060	1.151	0.144	0.680
Central Bank of India	67.3	11.539	2.309	0.158	1.921	0.508	0.990	0.291	0.850
Corporation Bank	29.2	13.713	2.266	0.157	0.630	1.166	1.081	0.180	0.600
Dena Bank	32.5	11.770	2.402	0.180	1.902	0.810	0.826	0.455	0.550
IDBI Bank Ltd	104.7	13.358	0.934	0.572	1.262	0.692	0.848	0.278	0.720
Indian Bank	53.4	13.446	3.106	0.171	0.807	1.388	1.089	0.199	0.800
Indian Overseas Bank	62.8	13.349	2.691	0.144	1.329	0.937	1.102	0.044	0.740
Oriental Bank of Commerce	66.8	12.151	2.316	0.163	1.138	1.092	0.939	0.058	0.580
Punjab and Sindh Bank	12.4	12.589	2.656	0.147	1.796	0.774	0.593	-0.101	0.800
Punjab National Bank	269.3	13.160	3.016	0.182	0.812	1.200	1.452	0.187	0.580
State Bankk of India	1431.7	12.957	2.703	0.163	1.881	0.906	1.776	0.188	0.620
Syndicate Bank	60	12.138	2.524	0.169	0.968	0.843	1.009	0.256	0.660
Uco Bank	74	12.257	2.094	0.178	2.052	0.578	0.936	0.169	0.690
Union Bank of India	86.6	12.316	2.517	0.184	1.220	1.030	1.304	0.172	0.580
United Bank of India	17.4	13.113	2.369	0.152	1.812	0.627	0.720	0.120	0.820
Vijaya Bank	34.3	12.356	2.264	0.102	1.040	0.763	0.991	0.251	0.550

Panel B: New Private-Sector Banks

Bank	Market Cap (In Rs. Billion)	CAR	NIM	NII Growth	Net NPA	ROA	P/B ratio	Profit Growth
Axis Bank Ltd	686.2	13.538	2.453	0.390	0.581	1.433	2.754	0.411
HDFC Bank Ltd.	1796.2	14.769	3.779	0.320	0.343	1.507	4.052	0.314
ICICI Bank Ltd	1437.2	15.836	2.048	0.233	1.307	1.307	2.034	0.271
Iindusind Bank Ltd	263.7	13.288	2.244	0.286	1.338	0.976	2.252	0.478
Kotak Mahindra Bank LTD.	601.6	16.448	4.074	0.420	1.162	1.461	6.031	0.461
Yes Bank Ltd.	149.3	16.923	1.996	1.009	0.063	1.436	3.186	-1.420

Panel C: Old Private-Sector Banks

Bank	CAR	NIM	NNI Growth	Net NPA	ROA	P/B ratio	Profit Growth
City Union Bank Ltd	12.780	2.861	0.245	1.182	1.549	1.282	0.287
Development Credit Bank	12.742	2.373	0.221	2.490	-0.523	1.637	0.573
ING Vyasya Bank	11.918	2.432	0.208	0.831	0.644	1.639	1.303
Karnataka Bank	12.709	2.139	0.218	1.467	1.037	1.020	0.130
Karur Vyasya Bank	14.501	2.720	0.214	0.459	1.570	1.353	0.233
Lakshmi Vilas Bank	12.332	2.244	0.195	2.269	0.508	0.970	1.119
Sounth Indian Bank	13.318	2.530	0.229	1.094	0.890	1.034	0.967
The Dhanalakshmi Bank	11.068	2.270	0.206	1.712	0.201	1.169	-0.750

Source: CMIE Prowess and Authors' Calculations; Annual Reports

Table 2: Category-Wise Examples of Issues in Board Minutes

Category	Examples
Risk	At one meeting, the Board reviewed country risk management of the bank. The Board took note of country-wise exposures, their causes and steps taken to mitigate the risks. Following the advice of RBI from its Annual Financial Inspection, another board discussed a study concerning the implementation of a mechanism for evaluating concentration risk amongst Cash In Transit (CIT) agencies empanelled by the bank. The Board was briefed on the salient features relating to the CIT agencies on concentration risks identified, appointment, annual appraisal, recommendations etc. In another meeting, the Board was presented with the annual review of Market Risk & Derivative Policies covering various risk limits, monitoring and reporting arrangements of Market Risk, Treasury activities which was thereby approved.
Business Strategy	At one bank, the management sought approval for ratification for the introduction of a new retail loan product and also for delegation of powers for this specific product to branch managers from zonal managers. The Board ratified the proposals followed by specific directions regarding collection and verification of customer In another minutes, the management sought Board approval for Rupee Drawing Arrangement with two different international exchanges. The Board did not approve one of the proposals. One board undertook a strategic review of the areas like, Business Plan, Capital Planning, Performance under Priority Sector advances, Performance under Lead districts, Non-fund business and prospective business/product lines and closure of existing ones. In another bank, the senior management presented the strategy on liability and asset to the Board who stressed the need for adequate training of the concerned staff for a successful strategy. The Board also stressed to improve the turnaround time on credit to enhance customer service. At another bank, the Board was updated on the underwriting commitments for loans entered into by the Investment Banking division during the previous fiscal year and current half year.
Financial Reporting	The Board reviewed the banks credit/debit/prepaid card operations. The Board was briefed on the industry snapshot, product and portfolio update, customer service indicators, KPIs, new initiatives and strategy going forward. Performance review related issue common to all banks is the review of financial statements for previous quarter end. At another bank, the Board reviewed the P&L accounts of branches for quarter end June 2013.

Regulation and Compliance	Following RBI directions for reporting on monthly basis on Overseas Regulatory violations, the Board of a bank reviewed the same for the banks overseas branches. At another bank, the Board was updated on the actionable for banks based on findings of the Thematic Review on KYC/AML and sought comments from the Audit & Risk Management committees of the board before final submission. In one instance, the Board of a bank considered a note on appointment of designated director under PML Act, 2002 who will be responsible to ensure overall compliance by the bank with the provisions of the Act. The Board further clarified the roles and responsibilities of the Chief Compliance Officer as the Principal Officer under the Act in regard of this new development. At a government-owned bank, the Board reviewed the implementation of Business Correspondent (BC) Model under Financial Inclusion Plan. Workmen Employee director however dissented with the proposal. In one instance, the Board resolved that the bank become a member and actively participate in the Aadhaar Enabled Payment System, a payment service offered by the National Payment Corporation of India and Unique Identification Authority of India. However, the Board desired that the cost of Aadhar Enabled Services be brought down by using technology. The Board of one bank was updated on the progress made by the bank in lending to the Micro and Small (MSE) sector in the current financial year. Appointment of board members, approving past minutes, choosing a chairman for the meeting, granting leave of absence.
Human Resources	In one meeting, the management sought Board approval for modification in the duration of compulsory leave required to be availed of by all officers of the Bank during a calendar year. The board further stressed that taking compulsory leave must be enforced on all officers and that during this period, the concerned officer should not have any access to his work desk. One of the directors of a bank in a meeting requested for the continuation of the guidelines regarding the appointment of Part-time Sub-staff and absorption of the PTS as Sub-staff which was thereby approved. At another meeting, approval was accorded for Performance Appraisal System (PAF) ratings & marks of officers in SMG Scale-IV to TEG Scale-VI be made accessible to the concerned officers. The Board however desired that, (i) TEF Scale-VII officers are to included in the proposal, and (ii) the reviewing authority gives opportunity to the officer to explain, if his/her marks are below the cut-off level for promotion and such an opportunity will be given in prospective cases.

Table 3: Issues Tabled in Board Minutes

Panel A: Issues Across Various Categories

Category	Public No. (% of total)	Private No. (% of total)	All Banks No. (% of total)
Risk	4 (9)	9 (14)	6 (11)
Business Strategy	16 (35)	21 (35)	18 (35)
Regulation and Compliance	17 (37)	22 (37)	19 (37)
Financial Reporting	5 (10)	7 (11)	6 (11)
Human Resources	4 (9)	2 (3)	3 (6)
Total Issues	45 (100)	59 (100)	51 (100)

Panel B: Debt-Equity Conflicts

Category	Public No. (%of total)	Private No. (%of total)	All Banks No. (%of total)
Minimisation of Risk	5(9)	9(14)	7(11)
Maximisation of Shareholder Value	24(45)	27(46)	25(46)
Regulation and Compliance	19(37)	22(37)	20(37)
Others	5(9)	2(3)	3(6)

Table 4: Issues Deliberated in Board Minutes

Category	Public			Private			All Banks		
	No. of Issues Deliberated (1)	As % of Total Issues Tabled (2)	As % of Total Issues Deliberated (3)	No. of Issues Deliberated (4)	As % of Total Issues Tabled (5)	As % of Total Issues Deliberated (6)	No. of Issues Deliberated (7)	As % of Total Issues Tabled (8)	As % of Total Issues Deliberated (9)
Risk	10	14.9	6.6	15	15.3	13.8	25	15.1	9.6
Business & Strategy	61	22.7	35.5	42	17.3	34.9	103	20.1	35.2
Regulation and Compliance	43	15.5	10.5	32	12.3	15.6	75	14.0	12.6
Financial Reporting	20	25.6	13.2	18	22.2	16.5	38	23.9	14.6
Human Resources	18	27.7	11.8	2	8.33	1.83	20	22.5	7.7
Total	152	20.1	100	109	15.5	100	261	17.8	100

Table 5: Bank-wise Number of Risk Committee Meetings and Composition during FY 2013-14

Name	Group	Risk Committee Meetings/Board Meetings	No. of Members	Constitution
Allahbad Bank	Public	0.24	5	CMD, ED, CA, SD
Andhra Bank	Public	0.36	8	CMD, ED, Gov, SD, OE
Axis Bank	New Private	0.83	5	Chairman Promoter, Promoter, MD&CEO, Ind
Bank of Baroda	Public	0.25	5	CMD, ED, Non-ED
Bank of India	Public	0.33	7	CMD, ED, part-Time
Bank of Maharasthra	Public	0.55	5	CMD, ED, RBI, Non-Ex
Canara Bank	Public	0.31	7	CMD, ED, OD, CA, SD
Central Bank	Public	0.27	8	CMD, ED, Gov, RBI, Part time
City Union	Old Private	0.24	5	Chairman (Non-ED), MD&CEO, Non-ED
Corporation Bank	Public	0.41	8	CMD, ED, Gov, WE, SD
DCB	New Private	1.17	5	Non-ED (Ind) , MD
Dena Bank	Public	0.33	6	CMD, ED, Gov, SD
Dhanalaxmi	Old Private	0.27	5	Chairman (Non-Ex Ind), MD&CEO, Ind Non-Ex
Federal Bank	Old Private	0.41	6	Chairman, MD&CEO, ED, Ind Non-Ex
HDFC	New Private	0.88	5	Ind Non-Ex Chairman, MD, Dep MD, non-Ex non-Ind, Ind non-Ex
ICICI	New Private	1.0	6	MD&CEO, Ind
IDBI Bank	Other Public	0.31	5	Ind , DMD
Indian Bank	Public	0.36	7	CMD, ED, WE, CA, SD, part time non-official
Indian Overseas	Public	0.41	5	CMD, ED, SD
IndusInd	New Private	0.57	3	Non-Ind Non-Ex, MD&CEO, Ind Non-Ex
Oriental Bank	Public	0.27	7	CMD, ED, Part-Time, CA
Punjab & Sind	Public	0.25	7	CMD, ED, Non-Official
Punjab National	Public	0.31	6	CMD, ED, part-Time Non-Official, SD
South Indian	Old Private	0.46	4	INE Chairman, INE
State Bank of India	Public	0.33	8	MDs, SD, Non-Official
Syndicate Bank	Public	0.46	8	CMD, ED, WE, Part-Time, SD
UCO	Public	0.38	8	CMD, ED, Gov, CA, OE, WE, Part-time
Union Bank	Public	0.21	9	CMD, ED, Gov, Part-time Non-Official, SD, WE
Vijaya Bank	Public	0.31	8	CMD, ED, Non-official, SD, WE, OE
Yes Bank	New Private	0.8	5	Non-Ex Non-Ind , MD&CEO, Ind

Source: Annual Reports of Banks

Table 6: Examples of discussion in Risk Committee Minutes

Panel A: Monitoring Issues

Issue Description	**Deliberation**
Interest Rate Risk in Banking Book for the quarter ended Dec 2012	The concerned department was directed to conduct sensitivity analysis under varying degree of interest rate shock and its impact on CRAR followed by back testing
Credit Portfolio Review As of June 30, 2013	The committee advised that Fortnightly report on the rating to be up to Executive Directors regularly
Impairment in Retail Loan Assets-Position as on June 30, 2013	The committee directed that mitigation measures proposed in respect of increase in NPA under *[blocked]* should be put up to the CMD. It also expressed concern about the increasing trend in NPAs and directed that those critical Zones/Regions where the increase in NPAs is comparatively higher than the rest of Bank, special area- specific efforts to be initiated and results should be monitored regularly
Review of Desired Portfolio Mix	The committee expressed its concern regarding low GDP levels of economy and existing percentage of High Risk internal rating category and thereby changed the desired portfolio limits for Totally internally rated accounts. It further directed that these limits be reviewed by the Credit Risk Management Committee every six months and to be placed before Board once a year
Key Risk Indicators-Upper Threshold Breaches Report	The committee desired that risk categorisation of the branches be reviewed. Further, all the thresholds limits be also reviewed by the respective divisions
Status of National Spot Exchange Limited transactions	The committee advised the Bank that it is critical to monitor the situation closely and take care of the interest of the investors with appropriate coordination with *[vendor/agency name blocked]*, though there may not be any direct financial impact to the Bank. Considering the tough economic environment and the likely higher inflation ahead, the Committee also advised that the Bank should closely monitor its mortgage portfolio especially in the light of likely impact of inflation on the Mortgage EMIs and so the resultant credit quality in case of Mortgage portfolio. The Committee appreciated the efforts being put in by the Management in the current situation and the presentation in such a short notice covering all areas likely to impact the Bank
Update on stress testing	The committee sought to know about the assumptions in stress testing scenarios of credit risk stress testing. While reviewing the results on liquidity stress testing enquired about the reasons for decrease in the cumulative gaps for bucket upto 28 days

Panel B: Ratification Issues

Issue Description	**Deliberation**
Credit Risk Management Policy 2013-14	The committee directed that the policy be vetted by an external consultant
Implementation of New Capital Adequacy Framework - Parallel Run reporting for the quarter ended March 2013	The committee directed to undertake revaluation of all assets every three years
Review of KYC Policy for 2013-14	The committee advised that obtaining the customer identification documents by the branch should be the beginning of KYC verification & the branch should be aware of the day-to-day transactions of the customer. It also suggested that may explore the possibility of compulsory checking of AMLOCK records by the Branch Manager may be on a weekly interval basis. It also recommended bringing out a booklet containing list of Do's & Dont's for branches for KYC
Ratification of Services provided to Co-operative Banks for facilitating payments of cheques at par	The committee suggested that the discussed business arrangement with co-operative banks be suitably incorporated in a standard agreement with separate clauses for completing the "Due Diligence" exercise and ensuring compliance with the KYC/AML norms
Ammendments to Investment Policy	A non-executive director enquired about the control framework in place for a business investment to which it was informed that the investment would be monitored within the existing investment limit, value at risk limit and stop loss limit stipulated in the Investment Policy
Modification to Underwriting and Loan Syndication Policy (UWLS)	The committee stressed that (i) a voting risk representative always be present and (ii) in the absence of CRO there should always be a senior risk representative in the risk UWLS committee
Early Intervention Mechanism - Increased scope of Special Loan Monitoring Group (SLMG) Resultant Modification to Credit Risk, SAP and Restructuring Policies	The committee did not agree to recommend for delegation of authority on Corporate Debt Restructuring Cases to A1 Global Mandate but recommended the rest of proposed modifications

Table 7: Bank Group-Wise Issues in Risk Committee Minutes

Panel A: Bank Group-Wise distribution			
Bank Group	No. of Issues Tabled	No. of Issues Deliberated	% Deliberated Issues
Public	22	5	22
Private	38	12	32
Average for all Banks	27	7.4	27.3

Panel B: Bank Group-Wise Decision Control				
Bank Group	Ratification)		Monitoring (%)	
	Tabled	Deliberated	Tabled	Deliberated
Public	72.0	9.3	252.0	219.5
Private	133.8	45.5	313.9	207.2
All Banks	228.8	62.0	565.8	412.5

Table 8: Forward Looking nature of Risk Committees

	Public	Private	All Banks
Total Sentences	1218	330	824
Forward Looking Sentences	24	143	206
Percentage of forward looking sentences	21.1	43.2	25.0