IdeaWatch

Barbara Casu of Cass Business School at City University of London and four coresearchers compared data on board and leadership diversity at large European banks against records of fines levied on those banks by the U.S. government since the global financial crisis of 2008. They found that banks with more female directors faced lower and less-frequent fines for misconduct, saving those institutions $7.84 million a year, on average.

The conclusion:

Banks with More Women on Their Boards Commit Less Fraud

Professor Casu, DEFEND YOUR RESEARCH

CASU: The result was clear and moderately strong: The financial institutions with greater female representation on their boards were fined less often and less significantly. We proved both correlation and causation by controlling for many other factors, including the number and dollar amount of fines received the previous year, board size, director tenure, director age, CEO tenure, CEO age, CEO turnover, bank size, banks' return on equity, and the volatility of the banks' stock returns. We even controlled for diversity itself. In other words, was the better behavior a function of boards' being more diverse in general—with members representing a variety of ages, nationalities, and both executives and nonexecutives—rather than because boards had more women? It turns out that gender diversity was what mattered—though I should acknowledge that other types of diversity contribute to fewer or lower fines, too.

HBR: Why look at fines levied on European banks by U.S. authorities? Two reasons. One, the data is really, really good. Any transaction in U.S. dollars can be reviewed and, if malfeasance is found, penalized by U.S. regulators, and folks have created amazing databases tracking violations. Second, it helps us avoid data that's been skewed by "regulatory capture"—that is, the lobbying and connections between banks and their domestic regulators. That's largely absent when you're looking at actions of U.S. regulators against foreign banks.

What types of offenses were committed? Banking and economic sanctions violations, money laundering, market manipulations, misleading or dishonest sales practices, tax and accounting fraud, and employment discrimination, among other things. We looked at all fines issued by all U.S. regulators and had information on the amounts, dates, offenses, whether sanctions were civil or criminal, and the sanctioning regulatory bodies.

Are we talking about a lot of bad behavior or only a little? Across the world from 2008 to 2018, the U.S. government levied about $500 billion in fines. That's half a trillion dollars.

Wow. So we need a lot more women on bank boards? Well, our research showed that you need a critical mass. If you have just one female director, the effect is quite weak. It's viewed as

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tokenism, and it's quite hard for one person to challenge existing corporate behavior. We found that you need at least three women to change the dynamic inside a board. We also found that the effect is even stronger when you have both female directors and women in executive positions at banks. We think that gender diversity in both areas is critical.

Is this evidence that women are just more ethical than men? That certainly could be one explanation. Women tend to be nurtured from a very young age to be more caring, accommodating, and nice, whereas men are often rewarded for being aggressive and ambitious and seeking personal gain. Women could also be more risk-averse, which would cause them to speak out when something—like committing fraud—seems dangerous. We also know that there's a gender punishment gap: Women are punished much more harshly than men for the same infraction. That might cause them to be more vigilant about stopping fraud; not speaking up carries much greater consequences for them. That's where we want to take this research next—to understand if women are behaving more ethically or if they're ethically similar but more risk-averse. The answer is probably some combination of the two.

What else might female board directors do better than men? We're not arguing that women are better than men—simply that they bring a different skill set and contribute to better monitoring and risk management. They're good for business.

How have men reacted to your research? You get a few ridiculous reactions. One person said to me, "You can push this all you want, but in the end children prefer to be with their mothers"—suggesting that women belong at home with the kids, not on boards.

Ugh. But that was the exception rather than the rule, right? The most common response was the immediate "Not all men are untrustworthy!" And of course, that's true. But we looked at billions of dollars in fines for egregious schemes in an industry that's more dominated by men than any other and found this positive effect with gender diversity at the board level. That's all we're saying.

If gender diversity works—if it saves a company from fraud and fines—wouldn't the market naturally move that way? Well, there are implementation costs, especially in the short term. Some research on gender quotas for boards has latched on to this. In particular the transition to more diversity incurs costs, including for the search for board members and recruiting, onboarding, and less obvious things like building the relationships needed to function as a team. And when you finally have a more diverse group, there are more points of view, more negotiations, and more compromise, so decision-making takes longer. Do those costs outweigh the benefits? I don't think so, but it's something people use to rationalize the status quo. So if we wait for the market to move naturally, for the culture to evolve, we may never get there. That's my belief. You need to force the issue.

Interview by **Scott Berinato**

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