

INTERLOCKING DIRECTORATES AND CITIGROUP'S EIGHT LINKS WITH THE MORTGAGE CRISIS

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ABSTRACT

This paper examines the links among interlocking board members of major banking institutions, particularly Citigroup, and the potential for strategic relationships and social networks to affect sources of information and networking that could have affected the buying of sub-prime mortgage packages.

Keywords: Interlocking directorates, board of directors.

INTRODUCTION

*“They sit on the boards of the largest companies in America. Many sit on government committees.
They make decisions that affect our lives. They Rule.”*

In the past few years, one of the largest monetary crises in American history has quickly developed and grown into a worldwide economic breakdown, with home values and markets falling like never before except for the Great Depression. The sub-prime mortgage crisis, started by numerous participants and circumstances, has mushroomed into global disorder. Discovering what set in motion the mortgage crisis is not the purpose of this paper. It is to demonstrate a link between the interlocking board members of the nine major banking institutions involved, especially Citigroup, and how strategic relationships and social networks increase the probability that interlocks could have magnified the crisis. This paper will exhibit how interlocking directorates could be a source of information, through board networking opportunities, which led each of the nine entities to be involved in the buying of the sub-prime mortgage packages.

INTERLOCKING DIRECTORATES

According to Daft, an interlocking directorate is when a member of the board of directors of one company sits on the board of directors of another company [4]. These individuals are a communication link between boards, which influence policies and decisions. A direct interlock occurs when one board member is the link between two companies. When a director of company A and a director of company B are both directors of company C, there is an indirect lock. Domhoff defines interlocking directorates as linkages among corporations created by individuals who sit on two or more corporate boards [5]. In the broadest sense, a board member, a top executive or a close relative of a member of the board of directors or top executive of a corporation functions as a board member of another [6].

One of the major reasons for interlocking directorates is for class integration, which is mutual security for the benefit of a social class by its members. Serving board members identify possible director candidates who have similar backgrounds, characteristics, networks and beliefs, which serve to protect

the class welfare of board incumbents. In protecting the class welfare of each other, interlocks help to reduce uncertainty between the parties by the inter-corporation trade of capital, including confidential information and access to markets, which help to buffer the effects of environmental uncertainty [8]. Corporations and boards will appoint influential persons as board members and hope that the new board member will become sensitive to the company's interests and draw on these interests in their decision-making. Daft states existing research illustrates that, as the wealth of a corporation declines, direct interlocks within financial establishments increase [4]. Economic insecurity within an industry also has been correlated with more indirect interlocks between rival companies. These traits of interlocks, especially the possible trading of information between the eight Citigroup Board Members and their social and professional networks are the basis of this research.

THE BANKING CONNECTIONS

Every United States Corporation, that is publicly traded, is required to have at least three directors on their boards, with most large corporations having at least ten [7]. Each of the companies researched have more than ten, with many between 12 and 18 directors. The initial investigation of the nine banks was conducted through a web site called *They Rule* [7], which is a database that allows the creation of maps that connect boards of leading companies to each other and links each director to all of the boards to which they belong. The data were collected from the companies' web sites and SEC filings. Although the site was available using 2004 data, this was during the beginnings of the crisis, and today, the 15 Citigroup Board members include seven of the directors serving in 2004.

The following eight banks were the preliminary group that was used to connect to Citigroup's Board:

- Bank of America
- Goldman Sachs
- J.P. Morgan Chase
- Mellon Bank
- Morgan Stanley
- Merrill-Lynch
- State Street
- U.S. Bank Corp

After closer inspection of the connections, it became apparent that by using only eight 2004 Citigroup Board Members, all of whom remain on the board at the time of this writing except one, there were nine more financial institutions involved in the mortgage crisis that could be linked to them. In total, there were indirect links to seventeen financial organizations. The nine corporations not included in the first search are Wachovia, Lehman Brothers Holdings, Bear Stearns, Freddie Mac, Fannie Mae, Countrywide, Principle, Wells Fargo and Bank One.

THE NINE DIRECTORS AND THEIR CONNECTIONS

Franklin A. Thomas

Consultant for The Study Group has been on their board since 2005. He has been involved with nonprofits such as the September 11th Fund and the Friends of the Nelson Mandela Children's Fund. Through connections at Pepsi Co, Thomas is indirectly linked with Lehman Brothers Holdings by one link, to Wells Fargo, Goldman Sachs, Bank of America and Freddie Mac by two links, to U.S. BankCorp, Mellon Bank, Fannie Mae and State Street by three links, to J. P. Morgan Chase, Morgan Stanley, and Fannie Mae by four links and there are just five links to Mellon Bank and Bear Stearns. He

serves on the boards of Lucent Technologies and Alcoa in addition to Citigroup, where he has been a board member since 1970.

Kenneth T. Derr

Derr was the Chairman and Chief Executive Officer of the Chevron Corporation from 1989 to 1999 and has been on the board since 1987. He has been a member of the Council on Foreign Relations, the National Petroleum Council and the Hoover Institution Board of Overseers. Derr serves as a director for Halliburton Corporation and through this one board is connected to State Street, J. P. Morgan Chase, and Wells Fargo by three links and four links to Merrill Lynch. Derr sits on the boards of Calpine and AT&T also.

George David

Former president of United Technologies Corporation, the manufacturer of the Black Hawk Helicopters, David started his career with the Boston Consulting Group as a Management Consultant. He is a board member of CitiGroup, United Technologies and British Petroleum, plus a member on the Business Council and the Business Roundtable. As a member of the United Technologies Board he has links to Fannie Mae and Wells Fargo through one link, Principal Financial and Wachovia Corporation with two links.

John M. Deutch

Deutch has served as the Director of Central Intelligence, Deputy Secretary of the U.S. Department of Defense, and the Under Secretary for the U.S. Department of Defense and the U.S. Department of Energy. He has held numerous positions at M.I.T. where he is an Institute Professor today. He is involved in the Urban Institute as a Life Trustee, plus Resources for the Future and the Center for American Progress, both as a trustee. He has been on the board of CitiGroup since 1996. Deutch has a single link through Raytheon Corporation to State Street and a link to J.P. Morgan Chase by way of three links. He serves also on the boards of Raytheon and Cummins.

Richard D. Parsons

Parsons is the Chairman of Time Warner Inc. and has been there in several positions since 1991, plus sits on their board. He has been the Chairman and Chief Executive Officer of Dime Savings Bank of New York, General Counsel and Associate Director for the Domestic Council of the White House, Deputy Counsel to the Vice President, Office of the Vice President of the United States, Assistant and First Assistant Counsel to the Governor, State of New York, and a director of CitiGroup since 1996. He has only one link to Morgan Stanley. Parsons serves on the boards of Estée Lauder and Time Warner, Inc.

Robert E. Rubin

As the Chairman of the Executive Committee, Rubin has been on the board since 1999. His positions have included Secretary of the Treasury of the United States, Assistant to the President for Economic Policy, Co-Senior Partner, Co-Chairman, Vice-Chairman, Co-Chief Operating Officer and general partner for Goldman Sachs. Rubin has served as a member of the Harvard Corporation, Co-Chairman on the Council on Foreign Relations, on Insight Capital Partners Advisory Board, as a special advisor for Tincum Capital Partners, and Taconic Capital Advisors as a member of the advisory board. Rubin, through the Ford Motor Company, is associated to Bank One Corporation by one link and Goldman Sachs by three links.

Alain J. P. Belda

Belda has been the Chairman of Alcoa Inc. since 2001 and has held numerous positions there since 1969. He has served on the Conference Board, as a trustee and is a member of The Woodrow Wilson International Center for Scholars, The Business Council, the Business Roundtable, and the World Business Council for Sustainable Development, plus the World Economic Forum International Business Council. He is linked with Countrywide Financial by three links and those three boards are DuPont, Conoco Phillips and Lockheed Martin.

C. Michael Armstrong

Armstrong has been on the board at CitiGroup since 1989 and is the Chairman for the Board of Trustees at John Hopkins Medicine. He has been the Chairman of Comcast, Hughes Electronic Corporation, IBM, and AT&T. He has served as the President's Export Council, a member on the Council on Foreign Relations, the Schroder Venture Capital Advisory Board, and a Visiting Professor for the M.I.T. Sloan School of Management. Armstrong is linked through Comcast and Northrup Grumman to Merrill Lynch.

Each of these biographies can be found in numerous articles on the Internet, including the Citigroup Website [3]; however the AOL Finance Website was used [1]. *Business Week's* Website [2], lists not only each of the board members, but has also counted the number of board relationships that each has. The following is a list of the eight board members, listed above, and the number of associations *Business Week* found between them and their board associations:

| | |
|----------------------|------|
| Franklin A. Thomas | 71 |
| Kenneth T. Derr | 54 |
| John M. Deutch | 98 |
| Richard D. Parsons | 252 |
| Robert E. Rubin | 234 |
| Alain J. P. Belda | 194 |
| C. Michael Armstrong | 242* |

*Note: data will be updated for presentation at WDSI Conference.

These numbers do not take into account all of the professional acquaintances that these men have throughout the government and on major councils. Each one of these men has the ability to pass along everything from a harmless recipe to a great deal, like the mortgage packages, to each other in various situations. It would be impossible to definitively prove that the way that so many banks learned about the sub-prime mortgage packages were from their board associations, but there is enough circumstantial evidence to intimate a very high chance for this possibility.

Many more connections could be made if the links were followed beyond the fourth level and it would be possible to complete a full circle back to the initial link. Just by examining the eight board members' links mentioned, there are numerous connections to government agencies and committees, which would link with large insurance, media, and manufacturing entities.

CONCLUSION

Even though there are laws against direct interlocks with businesses in the same industry, these directors do not have to directly link and risk prosecution. They have enough indirect social and professional interlocks to promote their class and businesses very well. They do sit on the boards of the largest and

most influential companies in America. Many do serve on major government committees and make decisions that affect our lives. *They Rule!*

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