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Corporate governance and the board of directors: a qualitative-oriented inquiry into the determinants of board effectiveness

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SAMENVATTING

Deze doctoraatsthesis onderzoekt de determinanten van een doeltreffende raad van bestuur. De raad van bestuur wordt beschouwd als de hefboom inzake deugdelijk bestuur en steeds meer worden raden van bestuur verantwoordelijk gesteld voor het (wan)beleid van ondernemingen. De verschillende bedrijfsschandalen, waarvan sommige tot immense economische verliezen hebben geleid, doen vragen rijzen over de doeltreffendheid van raden van bestuur in het beschermen van de belangen van aandeelhouders en andere stakeholders. Als gevolg zijn heel wat van de recente hervormingen gericht op een deugdelijker bestuur via een betere werking van de raad van bestuur. Niettegenstaande algemeen aangenomen wordt dat de raad van bestuur van essentieel belang is voor de continuïteit van een onderneming, werd tot nog toe relatief weinig onderzocht hoe raden van bestuur in de praktijk functioneren. In vele landen blijven de raads kamers immers verborgen voor het publiek, wat ervoor zorgt dat raden van bestuur moeilijk te bestuderen zijn.

Onderzoek naar deugdelijk bestuur en raden van bestuur in het bijzonder wordt in grote mate beïnvloed door de agency theorie. Vanuit het agency-perspectief wordt de raad van bestuur beschouwd als een intern controlemechanisme, bestemd om (potentiële) belangenconflicten tussen aandeelhouders (principal) en het management (agent) te beheersen en hun belangen op één lijn te brengen. In een dergelijke optiek wordt de doeltreffendheid van een raad van bestuur gewoonlijk benaderd als de mate waarin een raad van bestuur in staat is onafhankelijk te opereren van het management, in het belang van de aandeelhouders. Structurele karakteristieken van een raad van bestuur (bijv. omvang, proportie interne/externe/onafhankelijke bestuurders en splitsing functies van voorzitter en CEO) worden in empirische studies gebruikt als proxies om de doeltreffendheid van raden van bestuur te onderzoeken. Op dit moment is er echter weinig overtuigend bewijsmateriaal voor handen dat aantoont dat dergelijke structurele maatstaven een aanzienlijke invloed hebben op de prestaties van een raad van bestuur of van een onderneming.

Deze doctoraatsthesis probeert een beter inzicht te verschaffen in de factoren die de doeltreffendheid van een raad van bestuur bevorderen, de manier waarop deze factoren met elkaar in verband staan en de mate waarin de (groeps)dynamiek in de raad van bestuur hierbij een invloed uitoefent. De thesis omvat in dit opzicht een onderzoek naar de interne werking en het feitelijk functioneren van een raad van bestuur en vormt zo een bescheiden poging tot het openen van de “black box”. Onze empirische studies richtten zich tot raden van bestuur van Belgische ondernemingen en verliepen volgens een zorgvuldig geselecteerde kwalitatieve onderzoeksmethodologie. Een “mixed methods research design” (waarin bestuurders uit beursgenoteerde en niet-beursgenoteerde ondernemingen alsook experts inzake deugdelijk bestuur betrokken waren) en een gevalstudie (van een raad van bestuur van een grote Belgische beursgenoteerde onderneming) leverden rijke inzichten in het complexe web van factoren die de doeltreffendheid van een raad van bestuur vormgeven.

In een eerste studie verkennen en identificeren wij de diverse criteria die potentieel de doeltreffendheid van een raad van bestuur kunnen bevorderen. Om dit te verwezenlijken, werd vooreerst een grondige literatuurstudie uitgevoerd. Empirische gegevens werden verzameld aan de hand van interviews, aangevuld met twee bondige vragenlijsten. De studie onthult drie belangrijke punten. Ten eerste tonen de bevindingen aan dat er een belangrijke kloof bestaat tussen enerzijds het beperkt aantal structurele maatstaven die consistent in de literatuur terug te vinden zijn en anderzijds de brede set van criteria die door de bestuurders zelf benadrukt worden. In het bijzonder stellen wij vast dat in de percepties van de bestuurders systematisch een aantal niet-structurele of ontastbare factoren als belangrijke ingrediënten van een goede raad van bestuur naar voor komen. Ten tweede suggereren de bevindingen dat de onafhankelijkheid van de raad van bestuur wellicht te veel benadrukt wordt, ten koste van het belang van diversiteit. Dit concept is tot nu toe grotendeels onderbelicht gebleven in de context van raden van bestuur. Ten slotte vinden wij ook dat de informatie waarover bestuurders beschikken en de leiderschapsstijl van de voorzitter bijkomende (rand)voorwaarden zijn opdat een raad van bestuur een effectieve bijdrage kan leveren in de strategie van en het toezicht op een onderneming. Door deze studie is het duidelijk dat heel wat aspecten van een

doeltreffende raad van bestuur onzichtbaar zijn voor de doorsnee onderzoeker en zo slechts in geringe mate gekend zijn. Onze bevindingen suggereren bijgevolg dat de ambigue resultaten uit eerdere onderzoek grotendeels te wijten zijn aan het negeren van een reeks structurele- en gedragsfactoren die in werkelijkheid de doeltreffendheid van een raad van bestuur mee bepalen.

De tweede studie bouwt verder op deze empirische bevindingen en onderzoekt - vanuit een theoretische invalshoek - hoe de verschillende criteria met elkaar in verband staan. Daarbij wordt speciale aandacht besteed aan het aspect diversiteit en aan de niet-structurele of ontastbare aspecten van het functioneren van een raad van bestuur. De studie omvat de ontwikkeling van een 'proces'-georiënteerd onderzoeksmodel voor de analyse van de doeltreffendheid van een raad van bestuur en integreert daarbij literatuur inzake deugdelijk bestuur met literatuur inzake de effectiviteit van groepen. In wezen volgt het model een input-proces-output benadering met drie belangrijke kenmerken. Ten eerste wordt de doeltreffendheid van een raad van bestuur (output variabele) gedefinieerd in relatie tot de taken die de raad van bestuur geacht wordt te vervullen. In het bijzonder benaderen wij een doeltreffende raad van bestuur als een raad die succesvol is in het uitvoeren van een tweevoudige rol, met name een strategische en toezichthoudende rol. Ten tweede wordt er veel belang gehecht aan de procesvariabelen, cohesie, debat en conflict normen. Wij suggereren dat deze een indirect effect veroorzaken van de input variabelen op de output variabele. Ten derde introduceren wij, naast de omvang en de onafhankelijkheidsgraad van de raad van bestuur, diversiteit als een bijkomende structurele input variabele. Daarnaast worden specifieke relaties tussen de verschillende variabelen vooropgesteld.

De derde studie onderwerpt het voorgestelde model aan een empirische toets via een gevalstudie. Gegevens voor deze gevalstudie werden verzameld op basis van verschillende bronnen: interne documenten, een schriftelijke vragenlijst en interviews met alle bestuurders van de onderzochte raad van bestuur. De resultaten van de gevalstudie suggereren twee belangrijke punten. Ten eerste tonen de bevindingen aan dat de structurele karakteristieken van een raad van bestuur fundamentele maar onvoldoende

voorwaarden zijn voor de doeltreffendheid van een raad van bestuur. In het bijzonder wijzen de bevindingen erop dat de competentie van de bestuurders alsook hun interactie veel essentiëler zijn. Ten tweede tonen de bevindingen aan dat de doeltreffendheid van de raad van bestuur in het vervullen van zijn rollen afhankelijk is van zijn relatie met de andere actoren (management en aandeelhouders) in de corporate governance driehoek. Daarnaast blijkt uit de bevindingen dat het initieel voorgestelde model eerder onvolledig is en dat het moeilijk is om de effecten van de geïdentificeerde variabelen, gebaseerd op theoretische assumpties, te isoleren.

Het onderzoek resulteert in de voorstelling van een ‘congruentie’ model voor de doeltreffendheid van een raad van bestuur. Dit model conceptualiseert de raad van bestuur als een open, sociaal systeem dat bestaat uit diverse componenten die op elkaar inwerken. Van essentieel belang in dit systeemdenken is de assumptie dat de verschillende componenten in overeenstemming moeten zijn. De componenten zijn de (i) input (de middelen die een raad van bestuur tot zijn beschikking heeft), (ii) processen (de interacties en de gedragingen van de bestuurders), (iii) output (de uitvoering van de taken), (iv) contingenties (relaties raad van bestuur-management en raad van bestuur-aandeelhouders) en (v) externe factoren. De basishypothese van het model is: hoe groter de graad van overeenstemming of ‘fit’ tussen de componenten, hoe groter de doeltreffendheid van de raad van bestuur, hetgeen gedefinieerd wordt als de mate waarin de feitelijke invulling van het takenpakket van een raad van bestuur overeenkomt met de verwachte invulling.

Deze doctoraats thesis levert verscheidene bijdragen tot de wetenschap. Een eerste bijdrage spruit voort uit het feit dat ons onderzoek gevoerd wordt in een niet-Amerikaanse context en gebruik maakt van een alternatieve onderzoeksmethodologie. Tot op heden werd het merendeel van de empirische studies naar raden van bestuur verricht op basis van steekproeven van grote Amerikaanse ondernemingen. Bovendien zijn deze studies geënt op een kwantitatieve onderzoekstraditie die gebruik maakt van secundaire bronnen. Ten tweede draagt ons onderzoek bij tot de literatuur inzake deugdelijk bestuur en raden van bestuur in het bijzonder, door het staven van een

indirecte piste, inclusief vernieuwende onderzoeksthema's, voor de studie van relaties tussen raden van bestuur en de financiële prestaties van een onderneming. Traditioneel onderzoek legt te veel nadruk op de directe relatie tussen raden van bestuur en de financiële prestaties van een onderneming, met conflicterende bevindingen tot resultaat. Dit laatste doet twijfels rijzen betreffende de verklarende kracht van dergelijke input-output modellen voor het onderzoek naar raden van bestuur. Ten derde gaat ons onderzoek in op de verscheidene oproepen in de literatuur om bij het onderzoek naar raden van bestuur een pluralistische theoretische invalshoek te hanteren (in plaats van enkel een agency perspectief). Tot slot levert ons onderzoek ook een bijdrage aan de literatuur in andere domeinen, vooral inzake "organizational demography", doordat wij de relevantie van bepaalde theoretische concepten en variabelen, die regelmatig aan bod komen in studies van groepen, in de context van raden van bestuur onderzocht hebben.

Deze doctoraatsthesis levert ook een bijdrage voor ondernemingen, de beleggers/investeerders en beleidsmakers. Voor ondernemingen vormt een beter begrip van de succesfactoren van een doeltreffende raad van bestuur een interessante bron voor het uitvoeren van evaluaties van de raad van bestuur. Daarnaast is het onderzoek ook relevant voor het selectieproces van (nieuwe) niet-uitvoerende, onafhankelijke bestuurders omdat de bevindingen het belang hebben aangetoond van een juiste mix van competenties in de raad. Naar institutionele beleggers en rating bureau's toe duidt dit onderzoek op het gevaar enkel oog te hebben voor structurele karakteristieken bij de beoordeling van de kwaliteit van het ondernemingsbestuur. De bevindingen onderstrepen de nood voor het verfijnen van de scoringscriteria en de wegingmethodologie in hun evaluatie-instrumenten alsook voor het toepassen van een flexibele benadering bij de evaluaties van raden van bestuur op een wereldwijde schaal. Tot slot is dit onderzoek ook relevant voor het beleidsniveau, dat sterk geïnteresseerd is in het stimuleren van een aangepaste corporate governance omgeving. Het onderzoek vormt een bescheiden poging om enig academisch bewijsmateriaal te leveren ter ondersteuning van huidige en toekomstige initiatieven of hervormingen op het vlak van deugdelijk bestuur. In het bijzonder suggereren de bevindingen om een brede (ook aandacht voor niet-structurele aspecten van deugdelijk bestuur) en flexibele (ook aandacht voor de strategische,

sturende rol van de raad van bestuur) invalshoek te hanteren bij het ontwerpen, aanpassen en opvolgen van aanbevelingen en codes inzake deugdelijk bestuur. Bovendien laten de resultaten ook toe te reflecteren over de kosten en baten van bepaalde maatregelen.

SUMMARY

This dissertation examines the determinants of board effectiveness. The board of directors is considered to be an important governance device and boards are increasingly being held accountable for the organisations they govern. High profile corporate collapses, leading to major economic losses, have raised serious doubt on the effectiveness of boards in protecting the interests of shareholders and other stakeholders. As a consequence, much of today's corporate governance reforms (codes and recommendations, regulation etc.) are directed at improving corporate governance through upgrading the board's functioning. Despite the fact that boards of directors are presumed to be vital for a company's survival, there is still relatively little known about the way boards actually operate. In most countries, boardrooms have been shielded from view, which makes them difficult to study.

Corporate governance and board research have mainly been influenced by agency theory. From an agency perspective, the board of directors is an internal control mechanism designed to address the conflicts of interest between managers (agent) and shareholders (principal) and to bring their interests into congruence. Stimulated by the dominance of the agency theory in corporate governance, board effectiveness has commonly been viewed as the ability of boards to act independently from management to protect shareholders' interest. Structural board characteristics (e.g. size, insider/outsider representation, CEO duality) are treated in empirical studies as appropriate and adequate proxies for understanding board effectiveness. However, there is little definitive and striking evidence that these structural measures have had considerable impact on board or corporate performance.

This dissertation aims at understanding the factors that contribute to the effectiveness of boards, how these factors interrelate, and the extent to which board processes have an impact. In this respect, it attempts to open up, as much as possible, the "black box" of actual board conduct by also examining the inner workings of boards of directors. Our field studies focus on boards of directors of Belgian companies and unfold along a

carefully chosen qualitative research methodology. A mixed methods research design (involving directors of both listed and non-listed Belgian companies as well as experts in the field of corporate governance) and a case study (a board of directors of a major listed Belgian company) provide rich insights into the complex web of factors which shape the effectiveness of boards.

In a first study, we explore and identify the variety of criteria that potentially contribute to the effectiveness of boards. For this purpose, we conducted an in-depth review of the corporate governance literature. Empirical data was gathered through interviews, complemented by two small questionnaires. The study raises three major points. First, the findings highlight a gap between the limited number of structural board measures consistently found in literature, and the broad set of criteria that is emphasized by the directors themselves. In particular, we found a systematic occurrence of a number of intangible or behavioural factors in directors' perceptions of what constitutes a good corporate board. Second, the findings suggest that the value of independence may be overemphasized at the cost of the broader issue of diversity. Still, the concept of diversity is to a large extent under-exposed in board research. Finally, we found that information and the leadership style of the chairman are two additional conditions under which a board of directors can make an effective contribution to the strategic direction and control of a company. What becomes clear by this study is that many aspects of board effectiveness are invisible to mainstream researchers and as such poorly understood. Our findings suggest that the ambiguity in current research evidence can, to some extent, be attributed to the ignorance of a wider range of structural and behavioural factors which actually shape the effectiveness of boards in performing their roles.

The second study elaborates these empirical findings by examining - from a theoretical point of view - the interrelationship between the different criteria while paying special attention to the more intangible aspects of board conduct as well as to the issues of diversity. This study encompasses the development of a process-oriented model of board effectiveness and integrates the corporate governance literature with literature on group effectiveness. In essence, the model follows an input-process-output approach and has

three main characteristics. First, board effectiveness (output variable) is defined in relation to the tasks the board of directors is expected to perform. In particular, we have defined an effective board as one that can successfully execute a dual role set, namely its strategic and monitoring role. Second, strong emphasis is placed on board processes. In particular, we have identified three intervening variables (cohesiveness, debate and conflict norms) which are suggested to mediate the effects of a board's input factors on a board's output. Third, next to board size and independence, the concept of board diversity is introduced as an additional structural input variable. Furthermore, specific relationships between the various variables have been proposed.

The third study empirically challenges our proposed model of board effectiveness by means of a single case study. Data was collected using multiple sources of evidence: documentation, a written questionnaire and interviews with all directors of the board under study. The results of the case study suggest two important issues. First, the findings show that structural board characteristics are a fundamental but insufficient condition for board effectiveness. In particular, they indicate that competent people and the interaction amongst people are more critical for the effectiveness of boards. Second, the findings show that the effectiveness of a board in performing its roles depends on contingencies which relate to the other actors (management, shareholders) in the corporate governance tripod. Besides, the empirical findings highlight the incompleteness of our predefined board model as well as the difficulties of isolating the effects of separate constructs stemming from theoretical assumptions.

The overall result of our studies is the proposition of a congruence model for board effectiveness. This model conceptualises the board of directors as an open, social system, made up of various components that interact with each other. Of key importance is the overall alignment between the specified components. The latter includes (i) input (board's resources), (ii) processes (interaction and behaviour amongst board members), (iii) output (board task performance), (iv) contingencies (board-management and board-shareholder interactions), and (v) boundaries (a set of external 'givens'). The basic hypothesis of this model is that the greater the total degree of congruence or 'fit' between

the components, the more effective the board will be - effectiveness being defined as the degree to which actual board task performance is similar to expected task performance.

This dissertation offers several contributions to management science. A first contribution stems from the study of boards of directors in a non-US context using an alternative research methodology. So far, mainstream board research has carried out using samples of large US corporations and is inspired by quantitative research traditions using secondary data sources. Second, our research contributes to corporate governance and board literature by documenting an indirect route, including novel research areas, for investigating board-performance links. Mainstream board research has tended to overemphasize the direct link between board characteristics and financial firm performance, resulting in conflicting results. The latter raises doubt on the explanatory power of input-output models for the study of boards. A third contribution provided by our research is the response to calls for board studies using a pluralistic theoretical lens instead of a single (agency) perspective. Finally, our research contributes to other research streams, in particular the literature on organizational demography, by examining the relevance of theory and a limited number of constructs, frequently applied in group and TMT studies, in a board context.

This dissertation also has important implications for practitioners. For companies, the findings on the key determinants of board task performance could serve the purpose of board evaluations. In addition, this research has practical relevance for the selection process of (new) non-executive, independent directors as it highlights the importance of having an appropriate mix of competences on board. For institutional investors and rating agencies, this research highlights the danger of limiting attention to structural board characteristics when assessing the quality of corporate governance at a company level. It stresses the need to refine the scoring criteria and weighting methodology of the screening devices as well as to apply a flexible approach when evaluating boards of directors on a global scale. And finally, this research is also of particular interest to policy makers, concerned about stimulating an appropriate corporate governance environment. The research is a modest attempt to provide some academic evidence for current and

future governance reforms. In particular, the findings suggest that a broad (with attention also paid to the ‘soft’ aspects of corporate governance) and flexible (with attention also paid to the board’s strategic role) approach should be used when designing, adapting and monitoring corporate governance codes. In addition, the findings suggest that policy makers should reflect on ways to balance the benefits and costs of governance reforms.

TABLE OF CONTENTS

1	INTRODUCTION.....	1
1.1	The board of directors : questions about its effectiveness	3
1.2	Research questions.....	6
1.3	Research approach	7
1.4	Structure of the dissertation	9
1.5	References.....	11
2	THE BOARD OF DIRECTORS WITHIN THE CORPORATE GOVERNANCE FRAMEWORK.....	15
2.1	Introduction.....	15
2.2	The board of directors at the heart of corporate governance	16
2.2.1	The concept of corporate governance	16
2.2.2	The organization of boards of directors	18
2.3	Why a board of directors? The basic theoretical perspectives.....	21
2.3.1	Agency theory	22
2.3.2	Managerial hegemony theory	22
2.3.3	Stewardship theory.....	24
2.3.4	Resource dependency theory	25
2.4	The board of directors within the Belgian corporate governance environment....	27
2.4.1	Ownership and control of Belgian companies	27
2.4.1.1	The 'dominant firm logic' paradigm.....	27
2.4.1.2	Shareholder structure and ownership concentration in Belgium	28
2.4.1.3	Implication of ownership concentration on managerial hegemony and agency theory	32
2.4.2	The board of directors of Belgian companies	33
2.5	Conclusion	36
2.6	References.....	37

3	METHODOLOGICAL CONSIDERATIONS.....	41
3.1	Introduction.....	41
3.2	The choice of a coordinated qualitative research methodology.....	42
3.3	Research strategy and methods associated with the first part of the research project	45
3.3.1	Research strategy: a mixed methods research	45
3.3.1.1	Definition	45
3.3.1.2	Strengths and weaknesses of a mixed methods research	46
3.3.1.3	Selecting the mixed methods research design	47
3.3.2	Methods.....	49
3.3.2.1	Data collection	49
3.3.2.2	Data analysis	54
3.3.3	Legitimation in mixed methods research.....	58
3.4	Research strategy and methods associated with the second part of the research project	60
3.4.1	Research strategy: a case study.....	60
3.4.1.1	Definition	60
3.4.1.2	Motivation for the case study strategy	61
3.4.1.3	Case study designs	62
3.4.1.4	Common prejudices against case study research and the actions taken ...	63
3.4.2	Methods.....	66
3.4.2.1	The single case study	66
3.4.2.2	Multiple sources of evidence	67
3.4.2.3	Documentation.....	71
3.4.2.4	Data analysis	72
3.5	Conclusion	75
3.6	References.....	77
4	IDENTIFYING KEY DETERMINANTS OF EFFECTIVE BOARDS OF DIRECTORS.....	81
4.1	Introduction.....	81

4.2	Theoretical background	83
4.3	Methods.....	89
4.3.1	Sample and data collection for the qualitative phase.....	90
4.3.1.1	Sample.....	90
4.3.1.2	Data collection	91
4.3.2	Sample and data collection for the quantitative phase.....	92
4.3.2.1	Sample.....	92
4.3.2.2	Data collection	93
4.4	Results.....	93
4.4.1	Qualitative analysis.....	93
4.4.2	Quantitative analysis.....	99
4.5	Discussion.....	105
4.6	Conclusion	109
4.7	References.....	110
5	DEVELOPING A PROCESS-ORIENTED MODEL FOR BOARD EFFECTIVENESS.....	116
5.1	Introduction.....	116
5.2	Explaining the inconclusive findings in board research	118
5.3	Differentiating boards of directors from other organizational teams.....	120
5.4	Presenting a theoretical research framework of board effectiveness.....	123
5.4.1	Defining board effectiveness	124
5.4.2	Cohesiveness and debate as intervening variables.....	128
5.4.3	The effects of board characteristics on board processes.....	131
5.4.4	The moderating role of conflict norms	136
5.4.5	Indirect effects of board characteristics : the board processes-task performance link	138
5.5	Limitations and boundary conditions of the model	139
5.6	Conclusion	142
5.7	References.....	143

6	BOARD EFFECTIVENESS IN PRACTICE: A CASE STUDY	152
6.1	Introduction.....	152
6.2	Background.....	153
6.3	Research design	155
6.3.1	Case study method	156
6.3.2	Sources of information.....	156
6.4	Presentation of the case study.....	157
6.4.1	The Company’s environment.....	157
6.4.2	The Company’s mission, strategy and activities.....	158
6.4.3	The Company’s financial position	160
6.4.4	The company’s governance structure	162
6.4.4.1	Shareholder structure	162
6.4.4.2	Board of directors	163
6.4.4.2.1	The composition of the board of directors.....	163
6.4.4.2.2	Board committees	166
6.4.4.2.3	Comparison with an average board of directors of Belgian listed companies	167
6.4.4.3	Management.....	167
6.4.4.4	Supervision and control	168
6.4.5	Concluding remarks	168
6.5	Analysis of the relationships between the determinants of board effectiveness. 169	
6.5.1	Board task performance as output.....	169
6.5.2	The key inputs: size and composition of the board.....	175
6.5.3	Board processes: transforming inputs to output.....	177
6.5.3.1	The effects of board size and composition on debate	178
6.5.3.2	The moderating role of conflict norms	183
6.5.3.3	The effects of board size and composition on cohesiveness.....	184
6.5.3.4	The effects of debate and cohesiveness on board task performance	188
6.5.4	Board roles and contingency factors.....	191
6.6	Discussion.....	194

6.7	Reconsideration of our research framework: a system view on board effectiveness	196
6.7.1	Basic systems characteristics	197
6.7.2	A congruence model for board effectiveness	198
6.8	Conclusion	200
6.9	References	202
7	CONCLUSION	207
7.1	Introduction	207
7.2	Main findings and conclusions	208
7.2.1	Insights into the key drivers of board effectiveness	208
7.2.2	The influence of board processes on a board's task performance	215
7.3	Implications of the study	219
7.3.1	Implications for management science	220
7.3.2	Implications for practitioners	223
7.3.2.1	Companies	223
7.3.2.2	Institutional investors and other market parties	225
7.3.2.3	Policy makers	227
7.4	Limitations of the study	230
7.4.1	Methodological limitations	230
7.4.2	Scope limitations	233
7.5	Directions for future research	234
7.6	References	240
8	APPENDICES	244
	Appendix 1: code list	244
	Appendix 2: case study protocol	248
	Appendix 3: questionnaires	256
	Appendix 4: detailed analysis of themes	258
	Appendix 5: frequency tables	261
	Appendix 6: the Company's corporate governance model	263

LIST OF TABLES

Table 1: agency theory versus stewardship theory	25
Table 2: summary of the basic theories and their view on the board of directors	26
Table 3: shareholder structure of Belgian listed companies	28
Table 4: shareholder structure of Belgian non-listed companies.....	30
Table 5: descriptive statistics on boards of directors in Belgium versus US and UK	35
Table 6: traditional comparison of quantitative and qualitative research methodologies.	44
Table 7: strengths and weaknesses of mixed methods research	47
Table 8: strengths and weaknesses of main techniques used in the first part of the study	50
Table 9: overview of the data analysis activities	57
Table 10: strengths and weaknesses of documentation as a source of evidence	67
Table 11: documents used in the case study	72
Table 12: (qualitative) sample per directors' role.....	91
Table 13: (quantitative) sample per group of respondents.....	92
Table 14: ingredients of a good corporate board - directors' perspectives	94
Table 15: descriptive statistics of importance rate for the full sample (N=150)	99
Table 16: descriptive statistics of importance rate for sub-samples	100
Table 17: descriptive statistics of corrigible rate for the full sample (N=75).....	101
Table 18: descriptive statistics of corrigible rate for sub-samples.....	102
Table 19: characteristics differentiating boards as teams	122
Table 20: a board of directors' role set	124
Table 21: key financial figures of the Company.....	160
Table 22: key figures on share performance.....	161
Table 23: the Company's shareholder structure	163
Table 24: composition of the Company's board of directors	165
Table 25: role of the Company's board in strategy	171
Table 26: benefits and risks of the Strategic and Business Development Committee....	173
Table 27: role of the Company's board in monitoring	174
Table 28: descriptive statistics on board diversity at the Company.....	176

Table 29: level of debate.....	178
Table 30: conflict norms in the boardroom.....	184
Table 31: cohesiveness amongst the board members	185
Table 32: board independence, diversity and cohesiveness.....	187
Table 33: debate, cohesiveness and board task performance	190
Table 34: information as key aspect of board-management communication	192

LIST OF FIGURES

Figure 1: research approach.....	8
Figure 2: the corporate governance framework.....	18
Figure 3: variants of the 1-tier board model.....	19
Figure 4: the agency and managerial hegemony perspectives on the relevance of boards.....	24
Figure 5: cumulative holdings of the five largest shareholders in Belgium versus UK ...	29
Figure 6: control of Belgian listed companies.....	30
Figure 7: control of Belgian non-listed companies.....	31
Figure 8: power relationships between shareholders and management.....	33
Figure 9: sequential exploratory design.....	48
Figure 10: two-dimensional mixed method sampling design.....	59
Figure 11: linking importance and corrigible scores of determinants of board effectiveness.....	103
Figure 12: overview of the research framework.....	123
Figure 13: the Company share compared to BEL20 and Euro STOKX.....	162
Figure 14: a congruence model for board effectiveness.....	200

1 Introduction

Since the mid-eighties corporate governance has attracted a great deal of interest. The initial impetus was given by the Anglo-American codes of good corporate governance, like the Cadbury Code (1992) in the UK, the Principles and Recommendations of the American Law Institute (1984) and the Treadway Commission (1987) in the US (Van den Berghe and De Ridder, 1999; Wymeersch and Hopt, 1997). By the nineties corporate governance had reached Continental Europe as well as other parts of the world. Different reasons are given to explain why corporate governance became so prominent on such a large scale: (i) the takeover wave of the 1980s, (ii) pension fund reforms and the growth of private savings, (iii) the worldwide wave of privatisation of the past two decades, (iv) deregulation and the integration of capital markets, (v) the East Asia financial crisis, which has put the spotlight on corporate governance in emerging markets, and (vi) a series of corporate scandals (Becht et.al., 2002). Especially, a number of corporate malpractices (Enron, Worldcom, Ahold, Marconi etc.) have recently triggered a fresh round of governance reforms. Basic principles and rules are being reviewed and strengthened in order to reinstall investor confidence. Several actions have been announced or installed to prevent similar failures in the future, the issue of the Sarbanes-Oxley Act being the most controversial legislative intervention in this respect.

In Belgium, the debate on corporate governance has been going on since the mid-'90s. Unlike in many other countries, the development was not driven by a financial crisis or corporate failures, although some incidents have probably led to a greater interest in corporate governance issues (Van den Berghe and Levrau (eds), 1998). More of a concern was the danger of gratuitously copying Anglo-American corporate governance recommendations without taking into account the particularities of the Belgian corporate governance environment (e.g. an overwhelming impact of controlling shareholders). However, there was also a growing awareness that Belgian companies would have to live up to high corporate governance standards in order to compete in a globalising capital market. In this respect, installing the proper corporate governance mechanisms provides

companies with a competitive advantage in attracting capital, reducing the financial risks for investors, and consequently, the cost of capital (Van den Berghe and Levrau, 2003).

Corporate governance concerned with setting priorities, delegating power and organizing accountability, is seen as an important means to wealth creation (Becht et.al., 2002). In particular, institutional investors strongly believe in the positive performance effects of good governance, and are important players in fostering and enforcing good corporate governance. As corporate governance has an impact on the financial risk of their portfolio, it became an integrated part of their investment strategy (McKinsey & Company, 2002; Nesbitt, 1995). But due to the fact that corporate governance structures and practices vary widely between countries and companies, investors need some way of codifying the complex web in order to compare risk/reward profiles of global investment recommendations on a common base. Not surprisingly, this development has stimulated the rise of numerous corporate governance ratings. The latter provides investors with a means of judging the level of corporate governance and are frequently used as a screening device in analysing and measuring the related risks when making an investment decision (Van den Berghe and Levrau, 2003; Mallin, 2001).

This direct relationship with practice has incontestably stimulated academic research (Shleifer and Vishny, 1997). Corporate governance research is mainly concentrated around three topics: ownership and control (Becht and Mayer, 2001; Thomsen and Pedersen, 2000; La Porta et. al., 1999; Morck et.al., 1988; Demsetz and Lehn, 1985), boards of directors (see e.g. the review by Johnson et.al., 1996), and managerial issues (such as CEO succession, tenure and compensation) (Coles et.al, 2001; Zajac and Westphal, 1996 and 1995). In essence, the overwhelming majority of studies focus on the effectiveness of governance mechanisms available to protect shareholders' interest from (potential) managerial abuses in settings where organizational ownership and control are separated (Daily et.al., 2003). Simultaneously, the literature on corporate governance has been dominated by one theoretical perspective, namely agency theory. The latter provides a rationale for how a modern organization can be governed, given the assumption that managers are self-interested and in a context where they do not bear the full wealth

effects of their decisions (Jensen and Meckling, 1976). The manager-shareholder conflict is of particular relevance in countries where dispersed ownership is prevalent. Much of the theoretical thinking and research in governance has been, to a large extent, shaped by the observed developments in large US corporations. It may come as no surprise that the bulk of empirical studies are conducted in Anglo-American countries, driven by a US-oriented (quantitative) research tradition (Gabrielsson and Huse, 2005).

From these observations, the two-fold desire emerged (i) to investigate the effectiveness of one specific governance mechanism, namely the board of directors, within another setting, namely in a (Belgian) context which is characterized by concentrated ownership, and (ii) to better understand board practices by relying on a pluralistic theoretical lens and a qualitative research approach.

1.1 The board of directors : questions about its effectiveness

Questions about the governance of corporations, in particular the role and function of the board of directors, are very much alive today. Boards of directors are considered to be an important internal governance mechanism to safeguard shareholders' interest (Walsh and Seward, 1990) and they are increasingly held accountable for the organisations they govern (Hendry and Kiel, 2004). For years, boards of directors have been the subject of considerable scrutiny both in academic research and for the public at large (Van den Berghe and Levrau, 2004). High profile corporate collapses, leading to major economic losses, have raised serious doubts on the effectiveness of boards in protecting the interests of shareholders and other stakeholders (Taylor, 2003). A significant message was sent out by the Toronto Stock Exchange (1994) when it published its first corporate governance report entitled "where were the directors?". Given the fact that boards of directors are expected to independently monitor management and to provide corporate stewardship, it is not uncommon for many market parties to attribute, to some extent, the corporate failures to the inability of boards to operate effectively.

Stimulated by this practical relevance, much of the academic research on boards of directors has focused on whether boards are effective in aligning management and shareholders' interest, and derivatively, to what extent boards of directors contribute to a company's financial performance (Coles et.al., 2001). The dominant claim is that independent boards of directors are thought to be the most effective because their functioning is not compromised by dependence on the CEO or the organisation (Lynall et.al., 2003). As such, mainstream board research has been empirically investigating direct relationships between board structure and performance outcomes (Huse, 2005(a); Johnson et.al., 1996; Zahra and Pearce, 1989) while considering the number of board members, the insider/outsider ratio and CEO duality as important measures for board independence, and hence, effectiveness (Huse, 2005(b); Van den Berghe and Levrau, 2004; Leblanc and Gillies, 2003). Most studies have linked one or more of these board attributes to a measure of financial performance. A simple example is the relationship between the board size or the ratio of outside independent directors and company performance measured by Economic Value Added (EVA) (Coles et.al., 2001; Dalton et. al., 1998).

In addition, a second stream of research exists in which the composition of the board is linked to the performance of board roles. In particular, a board's monitoring effectiveness is well-studied using critical decisions - in the sense that these decisions involve a potential conflict of interest between management and shareholders - as a proxy. These critical decisions relate to CEO's total compensation, CEO's incentive pay, unrelated diversification, R&D expenditure, debt intensity, takeover defences and CEO turnover (see Deutsch, 2005 for a review). An important conclusion is that these simple direct input-output links have driven board research for almost two decades but have provided very little in the way of consistent findings (Daily et.al., 2003; Coles et.al., 2001).

In fact, mainstream board research is strongly influenced by a quantitative research tradition treating the board of directors as a "black box" (Huse, 2005(a)). The reason for this is that boards of directors are quite difficult to study. Of all the major institutions in society, they are probably the most closed and their workings have largely been shielded

from (public) view. The practical difficulties of investigating elite groups, such as boards of directors, have restricted the information that can be collected, and hence, the range of researchable issues. As a consequence, the vast majority of empirical studies have relied on easy retrievable data, available through annual reports, regulatory filings and corporate releases (Daily et.al., 2003). Only recently, a small subset of notable qualitative board studies emerged (e.g. Leblanc and Gillies, 2005; Huse et.al., 2005; Roberts et.al., 2005). Although previous research has enhanced our insights and knowledge on boards of directors, the findings of these recent studies have stressed the need to take another course in board research. For example, Roberts et.al. (2005) pointed out that a well-established body of research into corporate governance exists, based on the assumptions of agency theory, yet in comparison, our knowledge on how boards and directors actually behave or conduct their roles effectively is relatively limited.

While boards of directors are presumed to be vital for a company's survival, and attract much attention in practice (e.g. the many corporate governance codes and recommendations, corporate governance rating systems etc.), recent developments and initiatives are based on little robust evidence about significant board-performance relationships as well as on a poor understanding of how boards actually work (Leblanc and Gillies, 2005). In addition, there is a growing consensus both in literature and practice that progress in the field will largely depend on better insights into actual board practices, board processes and dynamics. This kind of research, however, highlights the need to consider alternative research methods, including various data collection and interpretation techniques (Huse, 2005(b)). Pye and Pettigrew (2005), for example, noted in their agenda for future research that "although it is some twelve years since Pettigrew (1992) first called for more process studies which address the dynamics of boards, their behaviour and outcome, the need for such work continues and is to be encouraged, for both academics and practitioners.... irrespective of the fact that such intangible matters are not easy to address, either theoretically and methodologically"(p.35).

1.2 Research questions

Our research tries to fill, at least to some extent, the gap observed before. In particular, this dissertation addresses **two main research questions**:

- 1) *What are the key factors that contribute to the effectiveness of boards of directors?*
- 2) *How do board processes influence the task performance of boards of directors?*

As previously noted, the board of directors is a common target in corporate governance reforms. Institutional shareholders, governance activists and many corporate governance codes advocate changes in board composition which are assumed to empower boards of directors and enhance their effectiveness (Westphal, 1998). In addition, numerous rating agencies have started to score the quality of corporate governance at a company level and the assessment of board of directors is consistently receiving high priority in this process (Van den Berghe and Levrau, 2003). It is striking to see that both market and academic interest is centred around the same limited number of structural board attributes, which Finkelstein and Mooney (2003) labelled the “usual suspects”, with the independence of boards of directors presumed to be the cornerstone of effective governance. At the same time, there is an increased awareness that an appropriate structure is an insufficient condition for boards of directors to add value and most studies on boards of directors are now being criticized for their narrow research approach (Gabrielsson and Huse, 2004; Daily et.al., 2003). The objective of the first research question – *investigating the main factors that potentially contribute to board effectiveness* – is **to identify** and **to explore** the **broad variety of criteria** that may influence the effectiveness of boards. In particular, the lack of consistent findings in traditional board research create the need to go beyond the established formal measures of board effectiveness in order to detect additional important criteria that may have been overlooked so far. Until now, mainstream board research has not provided a unanimous answer to the question ‘what

constitutes an effective board of directors’, and by consequence, no convincing evidence is provided on what to look for when assessing or evaluating the effectiveness of boards.

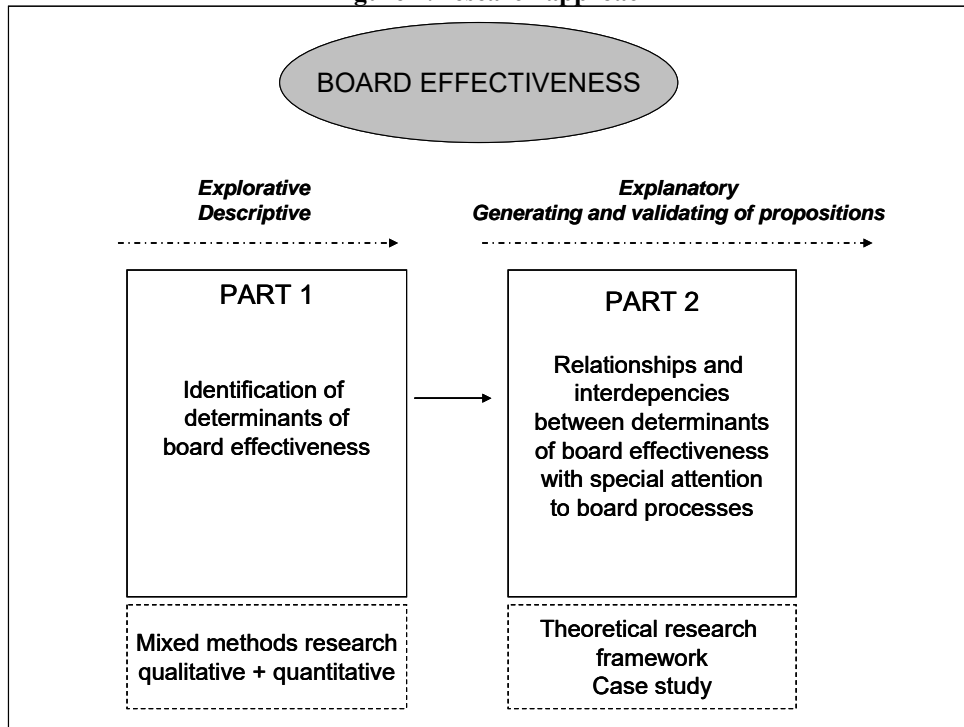
The second research question – *examining the influence of board processes on the task performance of boards of directors* – focuses on the more **intangible** and **behavioural** aspects of board conduct. The objective is to get a better understanding of how structural and non-structural factors are interconnected to form a complex set of interrelated criteria which actually shape the effectiveness of boards in performing their key tasks. The underlying rationale is that the overall emphasis on a limited number of structural measures implies a risk of assessing the effectiveness of boards in terms of form rather than substance. Unfortunately, too often, boards of directors are judged by living up to formal standards or benchmarks. Many of the corporate governance reforms lead to a kind of “box ticking” exercise with some superficial or cosmetic adaptations (Van den Berghe and Levrau, 2002). The failure of numerous companies has already proven that a narrow focus on compliance is dangerous because it creates a false sense of security. Similarly, there is a growing belief that effective boards of directors can only add value to an organization to the extent they are able to operate as a team (Nadler et.al., 2006; Huse et. al., 2005; Leblanc and Gillies, 2005; Conger et.al., 2001; Forbes and Milliken, 1999). This belief has engendered the need to pay more attention to the inner workings of the board of directors in order to better understand the influence of board dynamics on the effectiveness of boards.

1.3 Research approach

Boards of directors have been the subject of considerable research efforts. As explained in paragraph 1.1, two research streams prevail and show some common features: (i) the existence of significant relationships between the input and output variables is not systematically supported, (ii) agency theory appears to be the dominant underpinning theoretical perspective, and (iii) the empirical studies are characterised by an almost exclusive reliance on quantitative research approaches using secondary data (Daily et.al., 2003). Only very recently has a new stream of board research started evolving.

This dissertation links up with this new emerging direction and contributes to the literature on board of directors and the field of corporate governance more generally, by essentially proposing a new research approach and new research areas. Furthermore, this dissertation takes into account the fact that any research method needs to be closely interrelated with the nature of the research questions and the required level of analysis (Creswell, 1994). Hence, we have decided to realise our research objectives by means of a two-fold approach, as illustrated by Figure 1.

Figure 1: research approach



This dissertation is mainly characterised by a coordinated qualitative research methodology and - from a conceptual point of view - it can be broken down in two subsequent research parts. The first part corresponds with the first research question and objective, and is mainly intended to be explorative and descriptive. This part aims at getting a more in-depth insight into the ‘true drivers’ of board effectiveness in order to reveal some additional proxies for understanding the effectiveness of boards of directors. The research strategy that fits this purpose best, is a mixed methods research design (Teddlie and Tashakkori, 2003). The findings of the first part serve as an input for the second part which corresponds with the second research question. This part aims at

enhancing the knowledge on how multiple factors interrelate, and particularly, to what extent ‘board process’ variables impact board effectiveness. In order to obtain this objective, a theoretical research framework which - in essence - follows an input-process-output approach will be developed. Next, the identified relationships will be validated using a case study (Yin, 2003). As such, this part is mainly intended to be explanatory by empirically challenging our research framework and providing evidence for a new model for assessing board effectiveness.

The field studies focus on boards of directors of Belgian companies (listed as well as non-listed). Empirical data for both parts are gathered by several means. The most important source of data is a series of interviews with directors, and - to a lesser extent - with experts in the field. Taking into account the subjective nature of qualitative data, and particularly, the limitations of generalizability when using a case study approach, much attention is paid to the technique of triangulation (Jick, 1979). Moreover, the interpretation of data is guided and backboneed by theoretical perspectives and existing literature. In other words, throughout the whole dissertation there is a continuous interplay between theory and empirical findings.

1.4 Structure of the dissertation

Taking into account the two-fold research approach, the methodological choices involved and the chronological development of the research project, this dissertation reflects the following structure :

Chapter 2 introduces the research topic and clarifies the research focus. In particular, the chapter briefly presents the concept of corporate governance and describes how to frame the board of directors within its broader context. In addition, it discusses the prevalent theoretical perspectives which underpin board research. Finally, this chapter highlights the particularities of the Belgian corporate governance environment with respect to the ownership structure as well as to the structure and operation of boards of directors.

Chapter 3 provides a more detailed explanation of the methodology used to carry out this research project. The research strategies as well as the methods for the collection and analysis of the empirical data are discussed in detail.

Chapters 4, 5 and 6 represent the core of this dissertation and comprise three studies in accordance with our research approach. Chapter 4 presents the results of the first empirical study and provides descriptive information about the broad spectrum of factors that may contribute to the effectiveness of boards. In Chapter 5, a process-oriented model for board effectiveness is developed. This theoretical research framework reflects an input-process-output approach and draws on a variety of sources. Chapter 6 presents the case of the board of directors of a large Belgian listed company. The case study represents the second empirical study and is used to examine and validate the propositions derived from the theoretical research model.

Chapter 7 is the final chapter and provides, next to the overall conclusions, an overview of the implications of this research, the limitations, and the avenues for further research.

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2 The board of directors within the corporate governance framework

2.1 Introduction

As outlined in Chapter 1, much of the academic and public attention is directed to corporate governance, in particular to the role and function of the board of directors. The latter is commonly viewed as a critical governance device, but despite a well-established body of research, many aspects of board effectiveness are still poorly understood. The objectives of this dissertation reflect our desire to enhance the insights into board practices within a non-US setting. In essence, the research aims at understanding what factors contribute to the effectiveness of boards, how these factors interrelate and to what extent board processes have an impact. In this respect, it attempts to open up, as much as possible, the “black box” of actual board conduct by also examining the inner workings of boards of directors. Our field studies focus on boards of directors of Belgian companies and depart from the assumption that a board of directors matters for the host company. To further clarify our research focus, it is necessary to frame the board of directors within the broader context of corporate governance as well as within the specific Belgian corporate governance environment.

In this chapter, we first discuss the concept of corporate governance and indicate how the board of directors fits in the general corporate governance framework. Second, we touch upon the typology of board models to explain the way boards of directors are organized (in practice). Third, we describe the prevalent theoretical perspectives on boards of directors - as they provide the rationale for mainstream board research. Finally, we provide an insight into the particularities of the Belgian corporate governance environment with respect to the ownership structure as well as the board structure and operation. Understanding the Belgian context is useful because it differs, to a large extent, from the Anglo-American governance context where most of the studies on boards of directors have taken place.

2.2 The board of directors at the heart of corporate governance

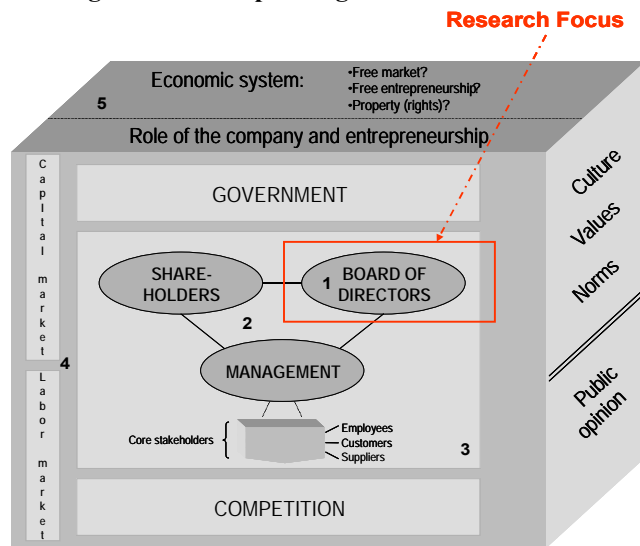
2.2.1 *The concept of corporate governance*

Although the concept of corporate governance has only emerged in the last two decades (Monks and Minow, 1996), it has exponentially entered the public domain. Still, there are widely divergent views on the nature of corporate governance and by consequence it is not easy to describe the concept unambiguously (Bain and Band, 1996). Shleifer and Vishny (1997) define corporate governance rather narrowly by stating that “it deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment” (p.737). John and Senbet (1998) propose the more comprehensive definition that “corporate governance deals with mechanisms by which stakeholders of a corporation exercise control over corporate insiders and management such that their interests are protected” (p.372). These two examples illustrate that the notion of corporate governance is perceived differently from one person to another and even across countries. Tricker (1993) stated in this respect: “corporate governance can mean many things to those concerned. Institutional investors have a different perspective from corporate regulators, board members from researchers. Insights can be drawn from the professional and theoretical worlds of organisational behaviour, jurisprudence, financial economics, accountancy and auditing as well as from the experiential worlds of director behaviour and board practices”(p.2).

To embody the varied approaches of defining corporate governance, Van den Berghe et.al. (2002) developed a hierarchical governance framework (see Figure 2). The simplest view on corporate governance focuses on the make up and operation of the *board of directors* (*level 1* in Figure 2). This is the central perspective of most codes and recommendations on corporate governance. Taken in a broader context, corporate governance is viewed from the angle of the so-called *corporate governance tripod* (*level 2*), whereby special attention is paid to the relationships between shareholders, directors and management. This angle relies to a large extent on the premise of separation of

ownership and control. It receives the most attention in economic research, in legal disciplines and in practice. From a modern management perspective, a more holistic approach at the corporate level is advocated (*level 3*) because companies are becoming increasingly structured in national and international groups. Global competition within the network and knowledge economy is giving rise to embedding companies in a cluster of networks with both suppliers and clients, while talent is becoming a scarce production factor. Therefore, greater attention is given to the company's core stakeholders (employers, customers and suppliers). From a socio-economic and chiefly political angle, a company is being forced to act as a corporate citizen (*level 4*). This perspective has broadened the purpose of corporate governance by including all kinds of stakeholders and ensuring a balanced weighting of their interests. In such an approach, no further distinction is made between levels 3 and 4 and one refers simply to the *stakeholder model*. The latter attaches much interest to the *sustainable* or *responsible* enterprise. Lastly, at *level 5*, corporate governance relates to the question of the primary reason for a company's existence. The fundamental question is whether a company's *raison d'être* is to create shareholder value or to create prosperity for all stakeholders involved. The Anglo-American corporate governance system favours the shareholder approach, whereas the broader stakeholder approach is more characteristic for the Continental European corporate governance system. Put differently, this level views corporate governance from a macro angle and refers to the national, European or the global level.

Figure 2: the corporate governance framework



Source: Van den Berghe et.al. (2002)

As demonstrated by this framework, the concept of corporate governance spans levels of analysis from within the company to the nation-state and beyond. Of importance for this study is the recognition that the board of directors is essential to most approaches of corporate governance (Cochran and Wartick, 1988). Although we focus our research on the board of directors, its embedding in the corporate governance tripod and the broader environment can not be ignored. Besides, when studying boards of directors one should be aware of the existence of different board models.

2.2.2 *The organization of boards of directors*

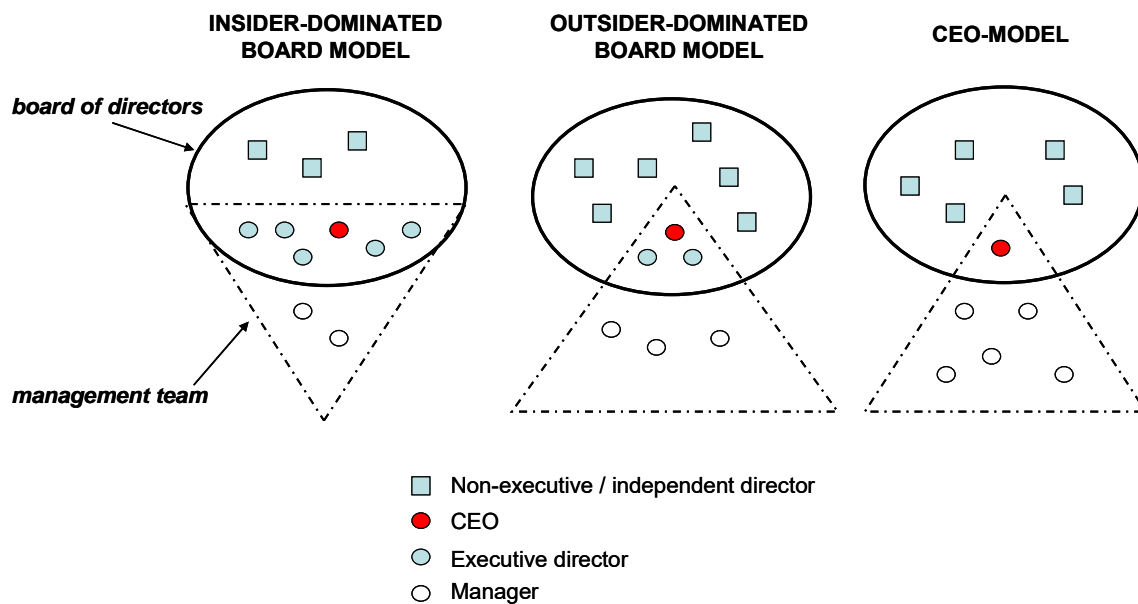
Boards of directors do not come as a single uniform body. They differ substantially between companies and countries. In essence, a typology of two board models can be identified namely the 1-tier or unitary board and the 2-tier or dual board.

In a **1-tier board model** executive directors and non-executive directors are sitting together in one organizational layer (the so-called unitary board of directors) (Maasen, 1999). Executive or inside directors are those who also fulfil a management function within the company. In contrast, non-executive directors come from outside the company

and some can be considered to be independent when they have no affiliations with the company, its shareholders nor its management (Van den Berghe and De Ridder, 1999). There are many variants that exist regarding the composition of a 1-tier board as illustrated by Figure 3:

- A) *Insider-dominated board model*: the board of directors is composed of a predominance of executive (inside) directors.
- B) *Outsider-dominated board model*: the board of directors is dominated by non-executive or independent directors.
- C) *CEO-model*: the CEO is the only executive sitting on the board of directors.

Figure 3: variants of the 1-tier board model



Source: adapted from Tricker (1998)

In addition, the leadership structure of 1-tier boards differs too. In some cases, the roles of chairman of the board and CEO are separated while in others the 1-tier board operates under CEO duality. The latter implies that the positions of CEO and chairman are combined. Board committees, such as audit-, remuneration- and nomination committees

are frequently installed by 1-tier boards in order to improve an effective operation of the board (Heidrick & Struggles, 2003; Egon Zehnder, 2003; Demb and Neubauer, 1992).

A **2-tier board model** is characterized by two organizational layers. The supervisory board (the upper layer) is entirely composed of non-executive directors. The latter may represent different parties such as employees, government, institutional investors etc. The management board (the lower layer) includes the executive directors (Maasen, 1999). In general, there is no overlap of membership between the two boards. In a 2-tier model, the executive managing director (CEO) is not allowed to act as chairman of the supervisory board. The legal separation of both bodies is a tangible way to distinct the responsibilities of managing and running the company from supervising and overseeing those responsible for the management function.

The distinction between the two board models is embedded in the **cultural and legal context**. The 1-tier board model is considered to be more shareholder-oriented and is internationally the most prevalence. It is by far the only board model in Anglo-American countries such as the US, UK, Canada and Australia. In Continental Europe¹, the 1-tier model can be found in Belgium, Italy and Spain. In contrast, the 2-tier board model is considered to be more stakeholder- or societal-oriented and is primarily found in some Continental European countries such as Germany, the Netherlands, Austria and Finland. In practice, the (legal) differences are often blurred as the two models tend to converge, to some extent, across the spectrum of firms and countries (Van den Berghe et.al., 2002; Maasen, 1999). Illustrative in this respect is the fact that large companies in countries with a 1-tier board regime delegate a substantial amount of their responsibilities to a CEO who is assisted by an executive committee. The latter resembles the executive board in a 2-tier board model. Pettet (2000) noted: “it might be argued that the way the UK boards have developed a de-facto division of function in recent years, means that while there are many technical differences between these and continental two-tier boards there is

¹ In France, Finland, Norway and Switzerland, an optional system exists, implying that the basic board model is either 1-tier or 2-tier while an (legal) option is foreseen of the other model. The option to choose between a 1-tier or 2-tier board model is also incorporated in the constitution of the European Company.

probably not much practical difference in the way companies are actually managed and monitored by directors” (p.22).

With respect to academic research on boards of directors, it seems that the distinction between the two board models has not been much of a concern to scholars. In fact, mainstream board research has focused on US boards and - to a lesser extent - UK boards, both being 1-tier in nature (Zahra and Pearce, 1989). Little research attention has been devoted to dual board models (Turnbull, 1997). In addition, the underlying theoretical assumptions in board research are in force irrespective of the way boards of directors are organized in practice.

2.3 Why a board of directors? The basic theoretical perspectives

As previously noted, this research departs from the assumption that a board of directors is of value-added for its host company, and hence, in our study the board of directors is considered to be an important governance device. Still, the actual impact of boards has frequently been criticized. Many corporate governance scandals, in the US and abroad, reinforce this criticism and questions arise whether a board of directors really matters for a company. An answer is provided by the basic theoretical considerations on the role of the board of directors. In fact, a variety of theories about what a board of directors is supposed to do, are underpinning the work of researchers in different disciplines (Hung, 1998). While agency theory dominates corporate governance research, managerial hegemony theory, stewardship theory and resource dependence theory provide additional theoretical foundations both as complements and contrasts to agency theory (Daily et.al., 2003). Based on the underlying assumptions, each theoretical perspective leads to other prescriptions regarding the role and structure of the board (see also chapters 4 and 5). In what follows, the basic theoretical drivers for studying boards of directors will be briefly discussed.

2.3.1 *Agency theory*

The dominant theoretical perspective in corporate governance and board research is agency theory (Daily et.al., 2003). Rooted in economics and finance, this theory reflects a conflict perspective as it is concerned with resolving problems that may occur in the relationship between two major parties, the principal (owner) and agent (the manager) (Jensen and Meckling, 1976; Eisenhardt, 1989). Agency problems stem from the fact that “managers who initiate and implement important decisions are not the major residual claimants (shareholders) and therefore do not bear a major share of the wealth effects of their decisions” (Fama and Jensen, 1983:5). Agency theorists believe that managers (agents) are self-interested and may pursue opportunistic behaviour that may be in conflict with the goals of the owners (principals). This behaviour may ultimately destroy shareholder wealth. In this respect, Hoskisson and Turk (1990) noted that: “managers who pursue their own best interests may select different strategies than managers who pursue the interests of shareholders and maximize firm value”(p.462). Agency theory attributes a key role to the board of directors as the latter is considered to be the “economic institution that helps to solve the agency problems inherent in managing any organization” (Hermalin and Weisbach, 2000:1). Put differently, the board of directors is one of the internal control mechanisms designed to address the conflicts of interest between managers and shareholders and to bring their interests into congruence (Walsh and Seward, 1990).

2.3.2 *Managerial hegemony theory*

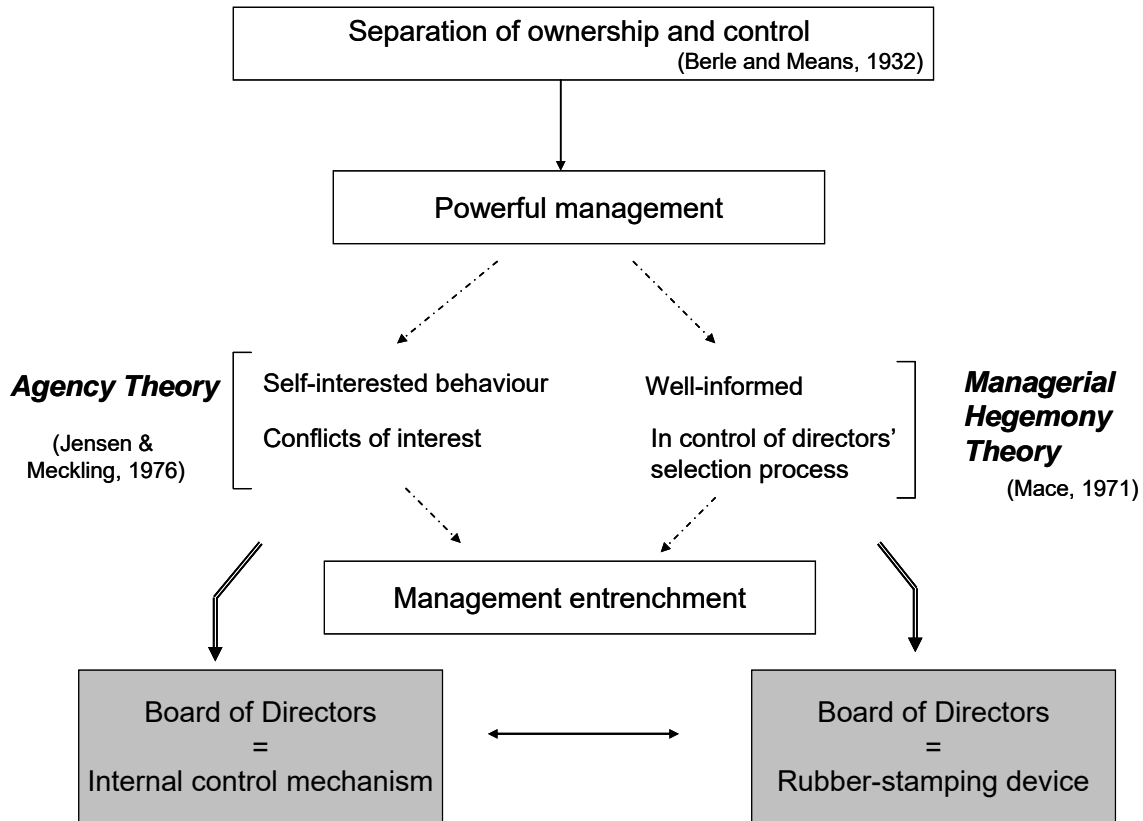
Not everyone has sympathized with the agency view on boards of directors. In fact, the extent to which a board of directors is of added value for directing a company has been subject to considerable debate since the seminal work of Mace (1971). In 1971 he published a study, demonstrating that the role of the board was in fact minimal. He found that boards of directors failed (i) to establish corporate objectives, policies and strategies, (ii) to ask discerning questions, and (iii) to select the CEO. The boards’ questionable

performance was also pointed out by Drucker (1974) who described the board of directors as “an impotent ceremonial and legal fiction...” and later by Lorsch and MacIver (1989) who noted that too many boards act more like pawns of their CEO rather than the potentates the law intended them to be. This common view of a rather passive, ineffective board of directors is frequently labelled as managerial hegemony theory. Succinctly put, this theory suggests that the board of directors is weak, dominated by better informed management, ineffective in alleviating conflicts of interest and only serves to approve proposals put forward by management, a phenomenon known as “rubber stamping” (Herman, 1981). In essence, the weakness and passivity of a board of directors is mainly attributed to its dependence on management (Kosnik, 1987). Boards are thought to be ‘creatures of the CEO’ whereby management plays a major role in designing the board (Patton and Baker, 1987). It is argued that the CEO has a considerable influence of the choice of directors whereby loyalty to the CEO instead of competence is decisive. Because directors owe their positions to management, they depend on the discretion of the latter for their re-appointment (Hart, 1995; Zahra and Pearce, 1989). Related is the argument that the benefits offered by a directorship stimulate directors to comply rather than to expose vigilant behaviour (Hendry and Kiel, 2004).

It must be noted that agency and managerial hegemony perspectives share the same starting point, this is the notion of separation of ownership and control. The latter has been first identified by Adam Smith (1776) in his commentary on joint stock companies and was further elaborated in the twentieth century by the influential work of Berle and Means (1932). They argued that the separation of ownership and control leads to a diffuse ownership in which the power of shareholders is diluted. The weaker position of shareholders affords management a greater level of control and provides a potential danger of management entrenchment. Although the two theories represent a managerial perspective, their views on the value-added of boards of directors differ substantially. Agency theory assumes that boards of directors will identify with shareholder interests and use their experience in monitoring and decision-making to prevent management of any self-interested tendencies. In contrast, managerial hegemony theory asserts that the power of the CEO, to select and compensate directors, refrains the board of directors

from taking up an active role in order not to put board seats and associated benefits at risk. Figure 4 illustrates agency and managerial hegemony perspectives on the relevance of boards.

Figure 4: the agency and managerial hegemony perspectives on the relevance of boards



2.3.3 Stewardship theory

Probably the most notable alternative to agency theory is stewardship theory, tapping insights from sociology and psychology (Davis et al., 1997). Proponents of stewardship theory argue against the self-interest opportunistic assumption of agency theory, claiming that managers are motivated by “a need to achieve, to gain intrinsic satisfaction through successfully performing inherently challenging work, to exercise responsibility and authority, and thereby gain recognition from peers and bosses” (Donaldson, 1990:375). Stewardship theorists perceive managers as good stewards of the company assets because

they have a range of non-financial motives which restrains them from misappropriating corporate resources at any price (Muth and Donaldson, 1998). A manager acts as a steward when he prefers working toward the best interest of the organization's collective needs. Such a manager identifies with the organization and considers organizational consequences of his decisions first and foremost (Davis et al., 1997; Block, 1996). In this respect, proponents of stewardship theory stress a board-management relationship based on collaboration, instead of control as accentuated by agency theorists. Based on these assumptions, the stewardship perspective prescribes a service role for the board of directors, calling for boards to advise and enhance strategy formulation (Sundaramurthy and Lewis, 2003). Table 1 presents a comparison between stewardship theory and agency theory.

Table 1: agency theory versus stewardship theory

<i>Agency Theory</i>	←————→	<i>Stewardship Theory</i>
	Assumptions	
Individualist Opportunism and self-interest	Human tendencies	Collectivist Cooperation
Extrinsic	Motivation	Intrinsic
Goal conflict (risk differential) Distrust	Management-owner relations	Goal alignment (firm identification) Trust
Control Distrust	Board-management relationship	Collaboration Trust
	Prescriptions	
Discipline and monitor	Board's primary role	Service and advise
Outsiders Non-duality	Board structure	Insiders CEO duality

(Source: adapted from Sundaramurthy and Lewis, 2003)

2.3.4 Resource dependency theory

From a different angle, resource dependency theory has also attracted the attention of corporate governance researchers. The resource dependence perspective, mainly

grounded in sociology and organizational theory, views a company as an open system, embedded in an environment comprised of other organizations on which the company depends (Pfeffer and Salancik, 1978). The central postulate of this theory is that external parties hold resources which a business organization perceives as crucial for the realization of its internal objectives. In order to acquire and maintain these resources, a company seeks to establish links with its environment, including competitors and other stakeholders (Zahra and Pearce, 1989; Pfeffer and Salancik, 1978). In this respect, a board of directors is considered to be a “cooptative” mechanism to access valuable resources that are inevitable for corporate success and to buffer the company against adverse environmental change (Hendry and Kiel, 2004; Pfeffer, 1972). Proponents of the resource dependency theory particularly advocate interlocking directorates and the appointment of representatives of important external constituencies to the board of directors as a means for obtaining critical resources. The latter may include: (i) advice and counsel, (ii) legitimacy, (iii) channels for communicating information to external organizations, and (iv) assistance in obtaining commitment from outside parties (Lynall et.al., 2003).

Table 2 provides an overview of the basic theoretical perspectives and their view on the role of the board of directors. For the sake of completeness, it must be noted that some other theoretical perspectives exist that have been applied in corporate governance and board research (see for instance the review by Hung, 1998). Our intent was not to provide a comprehensive list of the many theories apparent in the corporate governance literature, but rather to select and describe those perspectives that are most relevant within the scope of this study

Table 2: summary of the basic theories and their view on the board of directors

<i>Basic theoretical perspectives</i>	<i>Board of directors is viewed as ...</i>
Agency theory	An internal control mechanism
Managerial hegemony theory	A rubber-stamping device
Stewardship theory	A partnership model
Resource dependency theory	A “cooptative” vehicle

2.4 The board of directors within the Belgian corporate governance environment

2.4.1 Ownership and control of Belgian companies

As touched upon in Chapter 1, the major part of the existing schools of thought on boards of directors are developed within the Anglo-American corporate governance environment and closely linked to the Anglo-American model of corporation (Gabrielsson and Huse, 2005). The latter corresponds to the public company with dispersed ownership, as described by Berle and Means (1932).

2.4.1.1 The 'dominant firm logic' paradigm

Van den Berghe et.al. (2002) developed the concept of the 'dominant firm logic' to refer to those governance structures that are used as the reference base for developing theory, (national) laws, regulations and self-regulatory recommendations. In the US and the UK, it is well-documented that individual shareholders are widespread and neither institutions nor individuals hold a large proportion of shares in a company (Becht and Mayer, 2001). In these countries, corporate governance theorizing and policy making are primarily, if not exclusively, inspired by the 'Berle and Means' model of the publicly listed company. Yet, the influence of Berle and Means' analysis has been such that the notion of separation of control and dispersed ownership has been presumed to be universally applicable. It therefore became the dominant firm logic in corporate governance research around the world (Bebchuk and Roe, 1999; Roe, 1991). As such, the paradigm of the 'dominant firm logic' offers a plausible explanation why research on boards of directors strongly relies on a managerial perspective as reflected in the agency and managerial hegemony theories.

Meanwhile, the existence of quite different corporate governance environments has been documented (La Porta et.al., 1999; Franks and Mayer, 1992) and it is argued that the

Berle and Means' view on the corporation is much less applicable than previously thought. In particular, the separation of ownership and control is hard to maintain in Continental Europe as listed companies in most European countries show a remarkably high level of ownership concentration (Barca and Becht, 2001).

2.4.1.2 Shareholder structure and ownership concentration in Belgium

The evidence of concentrated ownership in (Continental) Europe also applies to Belgium. With respect to **Belgian listed companies**, the largest shareholder possesses on average 43,5% of share capital and the stake of the second largest shareholder is on average 10,5%. Table 3 provides an overview of the average shareholder structure of Belgian listed companies.

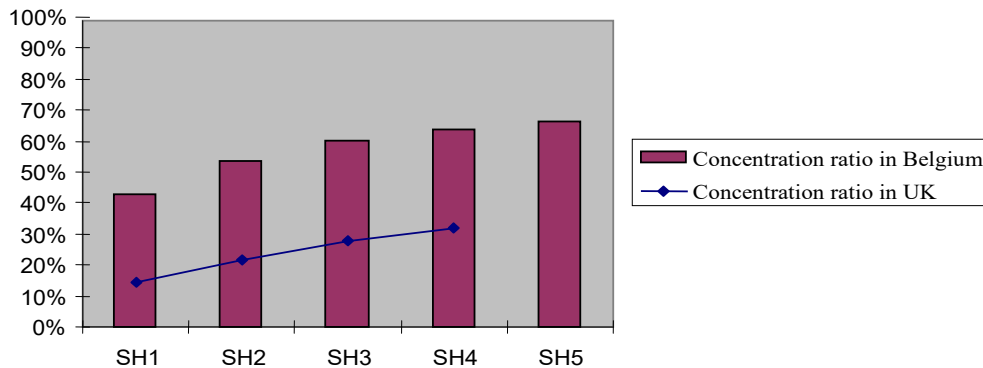
Table 3: shareholder structure of Belgian listed companies

	<i>Average</i>	<i>Median</i>	<i>Min.</i>	<i>Max.</i>
Largest shareholder (N=80)	43,48%	44,10%	3,55%	83,89%
Second largest shareholder (N=68)	10,55%	9,10%	1,04%	42,80%
Third largest shareholder (N=45)	6,68%	4,97%	0,47%	23,92%
Fourth largest shareholder (N=28)	3,69%	3,61%	0,15%	11%
Fifth largest shareholder (N=16)	2,76%	1,65%	0,12%	10%

(Source: Belgian Governance Institute, 2004)

In addition, Figure 5 illustrates the cumulative holdings of the five largest shareholders compared to results found in the UK.

Figure 5: cumulative holdings of the five largest shareholders in Belgium versus UK

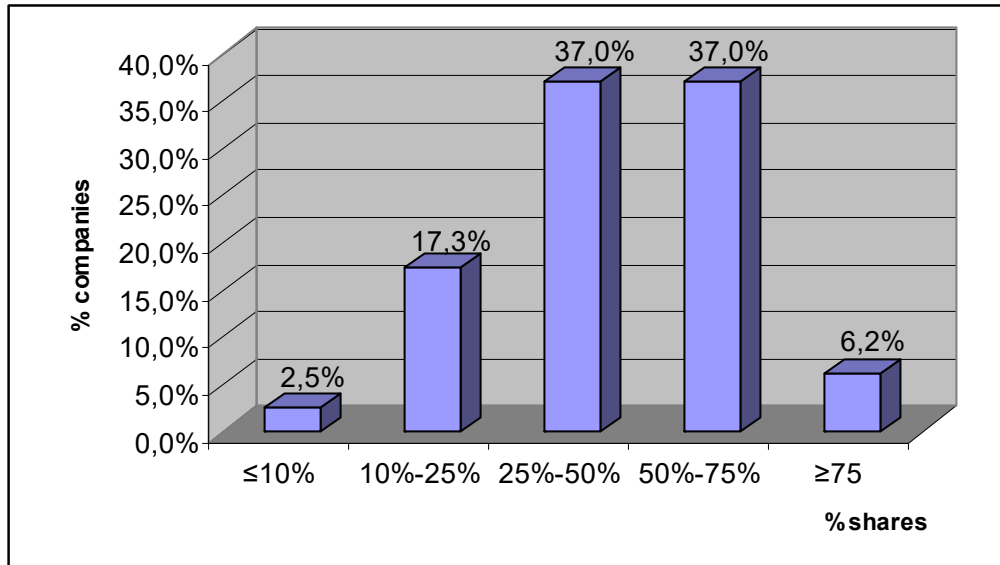


(Source: Belgian Governance Institute, 2004)

The concentration of ownership can also be studied from a different angle, namely the analysis of control (Becht and Mayer, 2001). More specifically, it is possible to provide insight into the number of listed companies that are controlled by a single shareholder. Control can be measured in different ways. From a legal point of view, a single shareholder controls a company when he holds at least 50% of the shares². However, a single shareholder can obtain control even with a direct stake less than 50%. This is the case when single shareholders, holding small stakes, form coalitions through voting pacts and similar arrangements (Van Der Elst, 2001; Becht and Mayer, 2001). Figure 6 presents the results for Belgian listed companies. 43% of Belgian listed companies are controlled by a single shareholder holding at least 50% of the shares. Moreover, a small number of listed companies (6%) have a dominant shareholder with a minimum stake of 75%. At 37% of the listed companies in Belgium, a major shareholder could be found with a participation in share capital between 25% and 50%. Taken together, 80% of Belgian listed companies have a ‘controlling’ shareholder.

² It must be noted that the principle of “one share-one vote” is in force in Belgium. This implies that a shareholder who holds at least 50% of the shares, obtains at least 50% of the votes.

Figure 6: control of Belgian listed companies



(Source: Belgian Governance Institute, 2004)

The findings for **Belgian non-listed companies** are even more striking³. The largest shareholder of non-listed companies in Belgium possesses on average 77,25% of share capital and the stake of the second largest shareholder is on average 19,1%. Table 4 provides an overview of the average shareholder structure of Belgian non-listed companies.

Table 4: shareholder structure of Belgian non-listed companies

	<i>Average</i>	<i>Median</i>	<i>Min.</i>	<i>Max.</i>
Largest shareholder (N=243)	77,25%	97,0%	0,3%	100,0%
Second largest shareholder (N=157)	19,10%	18,5%	0,01%	50,0%
Third largest shareholder (N=84)	11,37%	10,5%	0,1%	30,0%
Fourth largest shareholder (N=53)	7,70%	6,6%	0,1%	22,0%
Fifth largest shareholder (N=33)	5,60%	4,9%	0,1%	12,0%

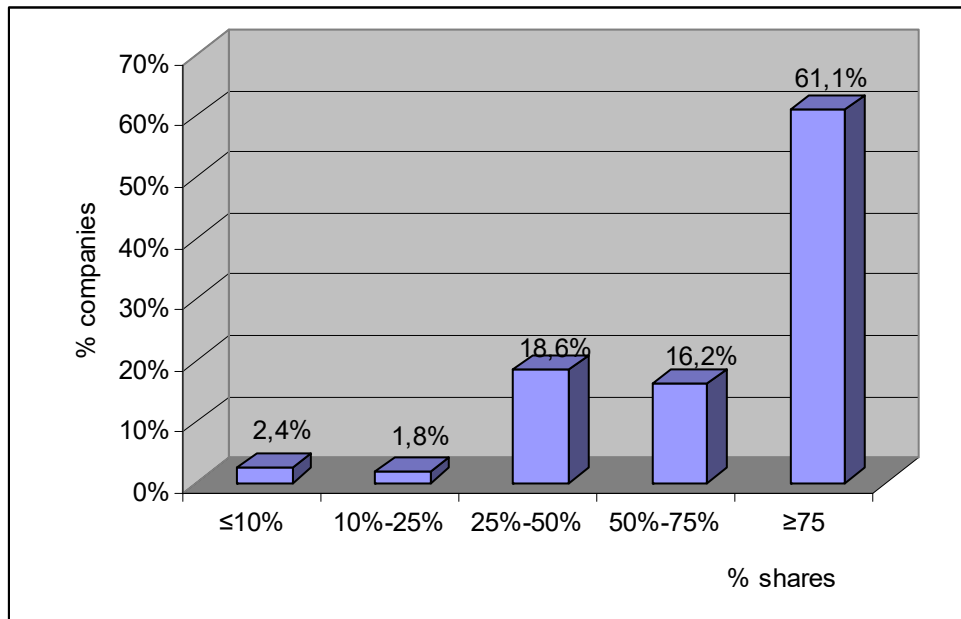
(Source: Belgian Governance Institute, 2005)

In addition, 77% of Belgian non-listed companies are controlled by a single shareholder, holding at least 50% of the shares. Moreover, a large number of Belgian non-listed companies (61%) have a dominant shareholder with a minimum stake of 75%. At 19% of

³ The sample consisted of 250 non-listed companies in Belgium.

the non-listed companies in Belgium, a major shareholder could be found with a participation in share capital between 25% and 50%. Taken together, 96% of Belgian non-listed companies have a ‘controlling’ shareholder. Figure 7 presents the detailed results.

Figure 7: control of Belgian non-listed companies



(Source: Belgian Governance Institute, 2004)

The descriptive statistics presented above, illustrate how the shareholder structure of Belgian companies differs substantially from the commonly accepted view on the ownership of corporations. Although ownership concentration is quite obvious with respect to non-listed companies, the findings for listed companies in Belgium suggest that widespread shareholdership is not commonplace. This has important implications on the relevance of some of the basic theoretical perspectives, in particular managerial hegemony and agency perspective, when studying boards of directors of Belgian companies.

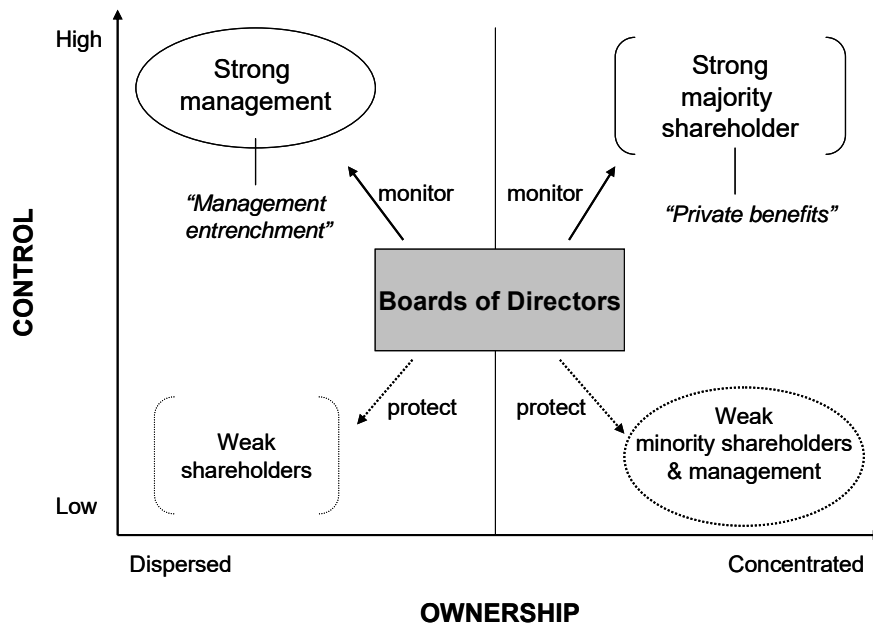
2.4.1.3 Implication of ownership concentration on managerial hegemony and agency theory

Managerial hegemony theory, which is to a large extent based on the assumption of an unrestrained power position of management to select and nominate board members, is suggested to be irrelevant in a context of ownership concentration. Two explanations can be given. First, concentrated shareholdership leads to a shift in power relationships. Unlike dispersed small owners, large shareholders are in a position to exert direct control over corporations and to influence actions taken by management (Denis and McConnell, 2003). By consequence, concentrated shareholdership leads to a shareholder control bias at the expense of management. Second, a very important feature of the Belgian corporate governance system is the fact that the nomination and dismissal of directors remains the legal responsibility of shareholders (Van Der Elst, 2006). This legal feature dilutes the power of management to influence the choice of directors and hence to ‘capture’ the board of directors.

Agency theory, on the other hand, is still relevant in a context of closely held companies but from a different angle. The issue at stake here is not the conflict relationship between owners and managers, but the conflicts of interest that may occur between the dominant shareholder and minority shareholders. In a context where shareholders hold a large fraction of equity, the problem of managerial control per se is not as severe as it is in a context of dispersed ownership. However, ownership by outside blockholders is not an unequivocally positive force from the perspective of the other shareholders because holders of large blocks of shares are in a position to engage in activities that benefit them at the expense of minority shareholders (La Porta et.al., 2000). The exploitation of the control position by a major shareholder to derive special benefits is referred to as “private benefits” (Van den Berghe et.al., 2002). Succinctly put, with dispersed ownership at one end and concentrated ownership at the other end of the spectrum of ownership and control, the nature of agency conflicts will vary accordingly to whom is in control. While dispersed ownership creates weak shareholders and strong managers, ownership concentration creates strong majority shareholders, weak managers and weak minority

shareholders (Gugler, 2001). In both cases an unbalanced power position exists, providing the potential for misuse of corporate resources and the occurrence of conflicts of interest. Therefore, boards of directors can be viewed as an important monitoring governance device. In addition, boards are considered to be instrumental for protecting a company's interest in general, and the interests of minority shareholders in particular (see Figure 8).

Figure 8: power relationships between shareholders and management



2.4.2 The board of directors of Belgian companies

In the previous section, we briefly described how the shareholdership of Belgian companies diverges from the ownership structure of companies in Anglo-American countries, and what the implications are on the basic theoretical perspectives. In what follows, we further document the differences between Belgian and Anglo-American contexts with respect to the composition and operation of the boards of directors.

The composition of the board of directors in Belgium. The average number of directors on boards of directors in Belgium is 10 for listed companies and 6 for non-listed companies. As for who sits on the board of directors, most boards include a mix of

executives, non-executives representing the shareholders and independent directors. The average number of independent directors varies between 3 to 4 for listed companies and 2 to 3 for non-listed companies. 29% of the boards of listed companies are dominated by independent directors which mean that the latter represents at least fifty percent of the board. With respect to non-listed companies, a majority of independent board members can be found in 14% of the cases represented. In addition, boards of directors are mainly crowded by men as female board members are rather scarce. Only 37% of listed and 40% of non-listed companies include at least one female director in their boards. Regarding the leadership structure of Belgian boards, 67% of listed companies and 61% of non-listed companies have already separated the roles of chairman and CEO.

The operation of the board of directors in Belgium. Boards of directors of Belgian listed companies meet on average 6 to 7 times a year. The corresponding number for non-listed companies is 4 to 5 times. Listed companies have also set up board committees, with remuneration by far the most popular (75%). Other committees include audit (69%) and nomination (37%). In contrast, board committees are less commonplace in non-listed companies. Audit- and remuneration committees were found in 15% of the cases while a nomination committee is set up in only 6%.

Differences and similarities of 1-tier board models between Belgium, US and UK. Although the three countries are characterized by a unitary board model, Belgian board practices differ from either US or UK practices with respect to key dimensions (see Table 5). First, the separation of the roles of chairman and CEO is definitely not the standard in the US where it is still subject to considerable opposition (Van den Berghe and De Ridder, 1999). Only a small percentage of US boards have abandoned CEO duality by splitting up the roles. Second, installing board committees has become more and more prevalent in US and UK practice, not in the least stimulated by recent (legal) proposals for corporate governance reforms (for example the Sarbanes-Oxley requirements). Third, because the perceptions of who is considered to be an independent director strongly vary according to the country involved (Van den Berghe and De Ridder, 1999), the statistics are less comparable with respect to the composition of the board. In contrast, similarities

between Belgian boards of directors and US, respectively, UK boards of listed companies are reported regarding the average board size and frequency of board meetings.

Table 5: descriptive statistics on boards of directors in Belgium versus US and UK

Country Key features	Belgium		US	UK
	Listed	Non-listed	Listed	Listed
Board size (average)	10,0	5,95	10,7	10,6
Separated board leadership structure	67 %	61%	29 %	97%
Composition of the board				
- ratio non-executive (NEDs) or independent directors (INDs)	NEDs 7 to 8/10 INDs 3 to 4/10	NEDs 4/6 INDs 2 to 3/6	n.a. INDs 8/10	NEDs 6/10 n.a.
- \geq one female director	37%	40%	88%	62,7 %
Board committees				
- audit committee	69%	15%	100 %	100 %
- remuneration committee	75%	15%	100 %	100 %
- nomination committee	37%	6%	98,5 %	98,7 %
Board meetings	6 to 7	4 to 5	6	7 to 8
<i>Data for</i>	<i>Year 2003</i>	<i>Year 2004</i>	<i>Year 2005</i>	<i>Year 2005</i>
<i>Sample</i>	<i>N=81</i>	<i>N=260</i>	<i>S&P 500</i>	<i>N=Top 150</i>

(sources: Belgian Governance Institute (2004, 2005); Spencer Stuart (2005))

The descriptives on board practices of Belgian companies presented above, provide a better insight into the extent boards of directors in Belgium resemble those frequently studied in Anglo-American countries. Especially, it must be noted that the research samples in mainstream board research commonly encompasses the Fortune 500 (or similar indices). These firms are important to the national economy, are the target of corporate governance reforms and provide the relative ease of data collection (Zahra and Pearce, 1989). However, these indices include the largest listed companies who operate within different legal environments and whose size exceed that of most Belgian listed companies. This observation is of relevance when assessing and comparing the findings of empirical research (see e.g. Chapters 4 and 6). From a different point of view, irrespective of the sample used, the descriptives in Table 5 also provide some evidence on how boards of directors, as a group, show some unique characteristics compared to other organizational groups (see Chapter 5 for a more detailed analysis).

2.5 Conclusion

This chapter has provided an insight into the concept of corporate governance and has positioned the board of directors as the cornerstone. Although it can be argued that equating corporate governance with the operation of boards of directors is far too narrow, a corporate board is presumed to be instrumental to the accountability of companies and the way companies comply with ethical and economic standards. Depending on the cultural and legal context, boards of directors are organized in many different ways but, in essence, they can be classified in two basic board typologies (1-tier and 2-tier). Up to the present, the unitary board model - which is assumed to be more shareholder-oriented - has received the most attention both in practice and literature. In fact, (1-tier) boards of directors are frequently portrayed as toothless watchdogs, dominated by management which do little to protect shareholders' interest. This description, if ever accurate in the past, is difficult to substantiate in the present. Different arguments can be put forward indicating that managerial hegemony is flawed. Increasing shareholder activism as well as legal and soft law reforms are only a few examples of forces strengthening boards vis à vis corporate management. Besides, this picture of ceremonial boards runs counter to other views, such as agency, stewardship and resource dependence perspectives, which consider the board of directors as an important governance device. In particular, one can not ignore the dominance of the agency perspective in both corporate governance research and debate. Consequently, boards of directors are commonly approached as internal control mechanisms for resolving conflicts of interest between "insiders" and outside investors. Who can be considered to be an "insider" (management or controlling shareholders) varies from country to country and is primarily dependent on the prevailing shareholder structure. Moreover, the shareholder structure is also considered to be a significant determinant of the way boards of directors operate. Therefore, when studying boards of directors, it is advocated to take into account the particularities of the corporate governance environment as well as to embrace a multi-theoretical approach for explaining the variety that is found in board composition and functioning.

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3 Methodological considerations

3.1 Introduction

The previous chapters introduced the objective of the research - examining the determinants of board effectiveness, the area studied - corporate governance, and the research focus - the board of directors. This chapter outlines the methodological considerations. The purpose is to provide an insight into the approaches used for collecting and analyzing empirical data, to describe the limits of the chosen approaches and to identify the sources of empirical data. As we discussed in Chapter 1, the dissertation is split up in two different but consecutive parts, in accordance with the two research questions.

(1) In the *first part*, which is based on the corporate governance literature, the variety of factors that potentially contribute to the effectiveness of boards of directors are identified. The purpose of this part is *exploration and description* in order to get a more in-depth insight into the ‘true drivers’ of board effectiveness. The findings serve as an input for the development of the theoretical research framework, which is presented in the second part of the research.

(2) The *second part* of the research tries to understand how the different factors interrelate and to what extent board processes have an impact on the task performance of boards of directors. For that purpose, a theoretical board model is presented and empirically challenged. This research part also includes literature on group effectiveness as well as top management team (TMT) literature and is mainly intended to be *explanatory*.

Although the two research parts require a different approach, they are characterised by a coordinated qualitative research methodology. This chapter starts with the clarification of

the general methodological choices and goes on to describe the research strategy and methods associated with both parts of the research project.

3.2 The choice of a coordinated qualitative research methodology

As noted in Chapter 2, mainstream research on corporate governance and boards of directors has primarily used quantitative methodologies in order to investigate causal relationships (see also Chapter 4). Moreover, within this quantitative research approach, the dominant data collection technique has been secondary or archival data, retrieved from public available documents such as annual reports, regulatory filings and corporate releases (Daily et.al., 2003). Only a small amount of studies opted for a field study approach using questionnaire data (notable examples are Johnson et. al., 1993; Judge and Zeithalm, 1992). In contrast, qualitative approaches have been very scarce until now. Some scholars studied boards through interview data (Roberts et al. 2005; Pettigrew and McNulty, 1998 and 1995; Demb and Neubauer, 1992; Lorsch and MacIver, 1989) while others were able to study actual board behaviour by direct observation techniques (Huse et.al., 2005; Huse and Schoning, 2004; Leblanc and Gillies, 2005 and 2003). However this kind of qualitative empirical research remains rare not in the least because of difficulties to get access to directors and the boardroom. Although the general trend in board research appears to be in favour of quantitative research, for the purpose of this research project qualitative research seems more appropriate.

Denzin and Lincoln (2005) offer a generic definition of qualitative research: it involves an interpretative, naturalistic approach to the world and it is inherently multi-method in focus. Put differently, qualitative researchers study things in their natural setting in an attempt to make sense of, or interpret, phenomena in terms of the meanings people bring to them. They seek knowledge through individual experiences of actors, who are directly involved in the phenomena under study. Miles and Huberman (1994) argue that this entails research conducted through an intense and/or extended contact with a 'field' or with life situations, trying to capture data on the perceptions of local actors "from the

inside”. Qualitative research is effective in capturing the complexity of social interactions in daily life and the meanings the participants themselves attribute to these interactions. The interest in daily practices in their own context and the meaning behind these practices take the qualitative researcher into a natural setting rather than laboratories (Denzin and Lincoln, 2005).

Still, qualitative research is difficult, rigorous and time-consuming and it should not be viewed as “an easy substitute for a quantitative approach” (Creswell, 1998:16). Researchers should balance the advantages and disadvantages of qualitative research and consciously indicate why the research topic is well-suited for a qualitative design. Several reasons can be advanced to explain the decision to adopt a qualitative research methodology. Above all, the *nature of the research questions* should demand a qualitative research approach (Patton, 2002; Creswell, 1998). Typically qualitative studies entail questions starting with how and what, in contrast to the why questions in quantitative research. The research questions described in Chapter 1, emphasize the importance of understanding how boards of directors actually operate and what drives their performance. They stress the need to look at mechanisms which provide *understanding* rather than predictions. Moreover, the methodology required for this kind of research calls for *interpretation* of the topic under discussion within a particular *context* (as indicated in Chapter 2). Maxwell (1998) suggests that qualitative research methods are particularly relevant for understanding meanings, contexts (which implies how events, actions, and meanings shape and are shaped by unique circumstances in which they occur) and processes (which means how events and actions take place over time) in their natural settings. Qualitative research does not intend to predict outcomes but rather to gain a deeper *insight into complex social phenomena*. In this respect, the richness and holism of the data generated by qualitative research provide a strong potential for revealing complexity and building a *holistic picture*. This is opposite to a single-angle and a distant explanation of the research problem. Another important feature of qualitative research is its *flexibility* (data collection times and methods can vary as the study proceeds) (see Table 6 for the traditional comparison of quantitative and qualitative research methodologies). Those are crucial arguments in the case of our research project.

In addition, the *access to the site* (applied to our study, access to boards of directors and board members) and the perspective of the researcher's role as *active learner* also encourage the selection of a qualitative research methodology.

Table 6: traditional comparison of quantitative and qualitative research methodologies

<i>Quantitative research methodology</i>	<i>Qualitative research methodology</i>
Philosophical assumption: positivism	Philosophical assumption : interpretivism and constructivism
Reality is objective and singular	Reality is subjective and multiple
No research process effects assumed; researcher is independent of that being researched	Recognition of the impact of the research process on the research situation; researcher interacts with that being researched
Presumed to be value-free and unbiased	Presumed to be value-laden and biased
Rule-driven research procedures	Flexibility in the research procedures
Quantification	Interpretation
Generalizations leading to predictions of cause and effect	Patterns, theories developed for understanding
Context-free	Context bounded
Accurate and reliable through validity	Accurate and reliable through verification

(Sources: Denzin and Lincoln, 2005; Cassel and Symon, 1994; Creswell, 1994)

Qualitative research genres have become increasingly important modes of inquiry for the social science and applied disciplines such as management, education etc. (Marshall and Rossman, 1999). Still, qualitative research is not a rose garden without thorns and in many cases, it has been marginalised as a supplement to core quantitative methodologies (Silverman, 1993). In particular, qualitative research has frequently been criticised as not being reliable due to the nature of the data it generates. Qualitative data is generally not easy to verify and it is difficult to observe and to analyze. Besides, most of the work is still done by the researcher (qualitative data analysis software already exists but it is still in its infancy compared to statistical analysis software, and its use requires plenty of time and efforts) and the quality of the results largely depends on the creativity and capacity of the researcher to manage the data. It often raises two problems : reliability (the uniqueness of a study within a specific context mitigates against replicating it exactly in another context) (Creswell, 1994) and anecdotally (brief conversations, snippets from

unstructured interviews are used to provide evidence of a particular contention) (Silverman, 1993). In order to limit these problems, objectivity and rigour were both crucial elements of attention during data collection and data analysis. Further limitations to specific research techniques are also discussed in the next sections.

3.3 Research strategy and methods associated with the first part of the research project

3.3.1 Research strategy: a mixed methods research

3.3.1.1 Definition

“A strategy of inquiry comprises a bundle of skills, assumptions and practices that researchers employ as they move from their paradigm to the empirical world. Strategies of inquiry put paradigms of interpretation into motion” (Denzin and Lincoln, 2005:25). They lead to the choice of specific methods of collecting and analysing empirical data. An important characteristic of research strategies is that they vary depending on the type of research. Besides, even within a type there is a variety of possible strategies. For example, qualitative research can involve case studies, observations, action methods etc. In contrast, quantitative research contains surveys, experiments etc.

The research strategy adopted for the first part of the research project is a *mixed methods research design*. Mixed methods research can be generally defined as the class of research which involves “the collection or analysis of both qualitative and quantitative data in a single study in which the data are collected concurrently or sequentially, are given a priority, and involve the integration of the data at one or more stages in the process of research” (Creswell et.al., 2003:212). In particular, it means that we adopt a research strategy, using more than one type of research method. It also implies working with different types of data.

3.3.1.2 Strengths and weaknesses of a mixed methods research

There seems to be a recent surge of interest in mixed methods research strategies⁴ and they are being increasingly used in some disciplines (Brannen, 2005). Different arguments are put forward in favour of mixed methods research. First, mixed methods research offers creative possibilities for addressing research questions in terms of a range of methods (Brannen, 2005). Second, mixed methods research is characterised by methodological pluralism or eclecticism, which frequently results in superior research (compared to mono-method research) (Johnson and Onwuegbuzie, 2004). Third, mixed methods research is useful in some areas because the complexity of phenomena requires data from a large number of perspectives (Sale et.al., 2002). Table 7 provides an overview of the strengths and weaknesses of mixed methods research.

Notwithstanding the many positive arguments, the use of mixed methods research is still subject to discussion. In particular, the “purists” in both qualitative and quantitative research advocate the incompatibility thesis. The latter posits that qualitative and quantitative research paradigms, including their associated methods, can not and should not be mixed (Johnson and Onwuegbuzie, 2004). However, many qualitative and quantitative researchers have reached basic agreement on several major points of earlier philosophical disagreement (see Johnson and Onwuegbuzie, 2004 for an overview of these issues). In essence, because the two approaches share the goal of understanding the world in which we live, it is stated that they can be combined in a study (Sale et.al., 2002). In addition, different scholars have demonstrated the successful use of mixed methods in their research which discredits the incompatibility thesis (Teddle and Tashakkori, 2005). Finally, others argue that research should not be preoccupied with the quantitative-qualitative debate, because it will not be resolved in the near future, while epistemological purity does not get research done (Miles and Huberman, 1984).

⁴ The last years there has been a growing number of international seminars and workshops devoted to the discussion of mixed methods research as well as the publication of new handbooks and articles in method journals.

Table 7: strengths and weaknesses of mixed methods research

<i>Strengths</i>	<i>Weaknesses</i>
Words, pictures and narratives can be used to add meaning to numbers, while numbers can be used to add precision to words, pictures and narratives.	More expensive and time consuming.
Can answer a broader and more complete range of research questions because the researcher is not confined to a single method of approach.	Some of the details of mixed research remain to be worked out fully by research methodologists (e.g. problems of paradigm missing, how to qualitatively analyze quantitative data, how to interpret conflicting results).
A researcher can use the strengths of an additional method to overcome the weaknesses in another method by using both in a research study.	Researcher has to learn about multiple methods and approaches and understand how to mix them appropriately. This can be difficult for a single researcher.
Can provide stronger evidence for a conclusion through convergence and corroboration of findings.	Methodological purists contend that one should always work within either a qualitative or a quantitative paradigm.
Can add insights and understanding that might be missed when only a single method is used.	
Can be used to increase the generalizability of the results.	
Qualitative and quantitative research -used together- produce more complete knowledge, necessary to inform theory and practice.	

(Source: Johnson and Onwuegbuzie, 2004)

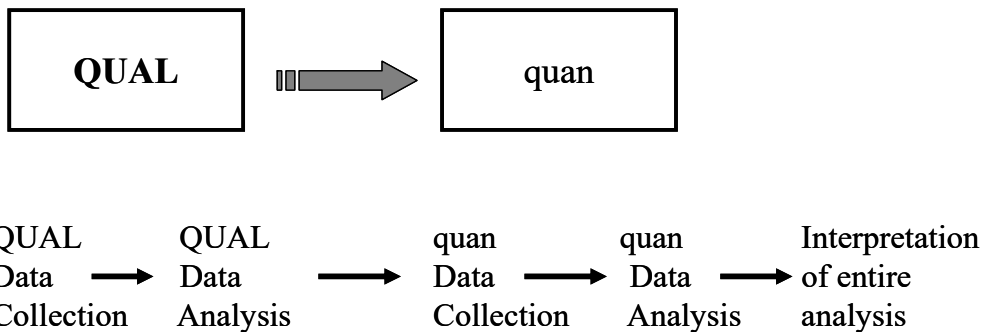
3.3.1.3 Selecting the mixed methods research design

In choosing a mixed methods research design that fits the purpose of the study best, some key dimensions must be considered (Creswell et. al., 2003). The first dimension relates to *the implementation of data collection* or the sequence that is used to collect both quantitative and qualitative data (concurrently or sequentially). The second dimension refers to the *priority* given to each form of data (equal status or emphasis on qualitative and quantitative data respectively). Third, the *stage of integration* in the research process

must be decided upon (e.g. integration can occur at any level, such as within the research questions, within data collection, within data analysis or during the interpretation of the results).

Using these three dimensions as a guideline in designing the most appropriate mixed methods research for the first part of the research project, we decided to opt for a *sequential exploratory design* (Creswell et. al., 2003). A specific feature of this design is the two-phase approach whereby the collection and analysis of the qualitative data in an initial phase is followed by a phase of quantitative data collection and analysis. In this respect, the qualitative phase provides the basis for the subsequent quantitative stage. More specifically, it determines the agenda for the successive quantitative research and it helps to develop the measurement tools. In our study, we use directors' open-ended responses during initial interviews to construct a rating survey for the second phase (see Chapter 4). Moreover, although both qualitative and quantitative data are obtained and used during the same research process, they do not receive an equal status. In contrast, we place most emphasis on the qualitative phase. The results of both data sets are then integrated during the interpretation phase. Figure 9 visualizes our mixed methods research design.

Figure 9: sequential exploratory design



Notation: "QUAL" stands for qualitative, "quan" stands for quantitative, "→" stands for sequential, capital letters denote priority

Source: Creswell, 1994

As the first part of the research project focuses on the identification of criteria that potentially contribute to the effectiveness of boards, we believe this sequential exploratory design is most suitable. The design allows us to explore the determinants of board effectiveness through a qualitative approach while the use of the quantitative data helps us in elaborating and interpreting the qualitative findings.

It must be noted that the sequential exploratory design differs from the classical use of the technique of triangulation. The term ‘*triangulation*’ is commonly used for the combination of qualitative and quantitative methods to address the same research problem (Morse, 2001; Jick, 1979). The archetype of triangulation strategies is corroboration or seeking convergence of research results (Creswell, 1994). In this respect, different methods are implemented concurrently and independently in order to confirm or cross-validate findings within a single study (Greene et. al., 1989). In contrast, our design is characterised by a sequential use of qualitative and quantitative methods whereby the first serves as an input for the development of the second. Moreover, the primary focus of our design is the exploration of a phenomenon by means of qualitative and quantitative data rather than concurrent validation. In sum, a mixed methods research design may serve many objectives. Besides corroboration, other ways of combining methods have been identified for the purpose of expansion, elaboration, initiation, complementarity, development and explaining contradictions (see Brannen, 2005 and Greene et. al., 1989 for a detailed explanation).

3.3.2 *Methods*

3.3.2.1 Data collection

Methods simply refer to specific research techniques that are used for collecting empirical data. There is a broad spectrum of methods available, ranging from direct observation and interviews to the analysis of artefacts and documents. Besides, methods can be combined. In the first part of this research project, two main techniques are

combined in order to gather the required empirical data: interviews (with directors of Belgian listed companies) and questionnaires (sent primarily to directors of Belgian non-listed companies and other actors in the field of corporate governance). Other techniques such as conference attendance as well as (roundtable) discussions with directors and actors in the field are also used. All the techniques have been selected in order to build a fair and solid picture of the variety of factors that potentially contribute to the effectiveness of boards. Although each technique has major advantages, there are also shortcomings inherent in every technique. Table 8 provides an overview of the strengths and weakness of the two main techniques used in this study. Both techniques are explained more in-depth in the following paragraphs.

Table 8: strengths and weaknesses of main techniques used in the first part of the study

<i>Research Technique</i>	<i>Strengths</i>	<i>Weaknesses</i>
Interviews	<p>Targeted – focuses directly on topic being studied</p> <p>Provide in-depth information</p> <p>Allow good interpretive validity</p> <p>Allow probing by the interviewer</p> <p>Useful for exploration</p>	<p>Bias due to poorly constructed questions</p> <p>Response bias</p> <p>Inaccuracies due to poor recall</p> <p>Reflexivity- interviewee says what interviewer wants to hear</p>
Questionnaires	<p>Good for eliciting content from research participants</p> <p>Can be administered to probability samples</p> <p>Can be administered to groups</p>	<p>Need validation</p> <p>Must be kept very short</p> <p>Response rate possible low for mail questionnaires</p> <p>Nonresponse to selective items</p> <p>Possible reactive effects (e.g. social desirability)</p>

(Sources: extracted from Yin, 2003 and Johnson and Turner, 2003)

- Interviews

The first main technique used in the present study is interviewing. Interviews can simply be defined as a “conversation with a purpose” (Fowler and Mangione, 1990). It involves

asking questions, active listening, interpersonal understanding, a respect for and curiosity about what people say (Marshall and Rossman, 1999). Interviews commonly target unobservable data such as feelings, thoughts, opinions and intentions (this reflects the meaning people attach to physical and social artefacts). They are instrumental to learn about phenomena or events that happen in the absence of the researcher (Patton, 2002). In total, 104 interviews were conducted with members of the boards of directors from Belgian listed companies. For more detailed information on this sample we refer to Chapter 4.

Type of interview. Interviews include a wide variety of forms ranging from individual to group interviews, from structured to unstructured etc. (Fontana and Frey, 2005). All interviews with directors of listed companies were carried out individually in a face-to-face verbal interchange (in the directors' mother-tongue) as part of a large scale in-depth study on corporate governance in Belgium. One main *standardized open-ended question* for the purpose of this research project was included in order to explore directors' own views on the most important criteria that constitute a good corporate board. According to Yin (2003) open-ended questions are well-suited to ask respondents about the facts of a matter as well as their opinions about the topic under discussion. In particular, the standardized open ended interview is based on "open-ended questions and results in qualitative data; at the same time, neither the wording nor the sequence of the questions on the interview protocol is varied, so the presentation is constant across participants" (Johnson and Turner, 2003:304). In this study, every director was asked the same question, at the same moment in the course of the interview, in order to compare the views of interviewees and to eliminate deviations between different investigators. In addition, the formulation of the question(s) should be carefully conceived to gather the data needed (Patton, 2000). We have opted to phrase the question in rather general terms as it allows room to probe for more sensitive aspects as well as to register directors' answers based on their broad experience in multiple boards of directors. The open-ended nature of the question involved, should provide us with a deeper understanding of how key actors in the field perceive the determinants of board effectiveness.

Multiple interview teams. Because the research includes an extensive number of directors involved in the interviews, the choice for multiple interview teams is justified to cover all respondents (Yin, 2003). The use of multiple interview teams minimalizes the likelihood of introducing bias into the study. In particular, the main open-ended question for the purpose of this research was asked in exactly the same way by the different teams and the answers were cross-verified by the other member(s) of the team(s).

No audiotapes. None of the interviews were formally tape-recorded while each interview was held, under the condition of anonymity of individual responses. Although recording has the advantage of interpreting answers in a more accurate way, two different actions are taken to guarantee a neutral and unbiased interpretation. First, detailed field notes were taken during each interview and electronically transcribed in a computer document immediately after the interview took place. Second, the majority of the interviews were carried out by a team of two interviewers. This allowed for mutual monitoring to make sure we were getting the most accurate data possible (Fink and Kosecoff, 1985).

- Questionnaires

Two short questionnaires are used as the second main technique, for collecting data. A questionnaire can be described as a self report instrument that is filled out by the research participants (Johnson and Turner, 2003). In total 150 respondents filled out the first questionnaire and 77 collaborated in the second questionnaire. For more detailed information on this sample we refer to Chapter 4.

Construction of the questionnaires. As outlined in paragraph 3.3.1.3 the questionnaires are part of the second (quantitative) phase in our sequential exploratory design. This implies that the findings of the first (qualitative) phase are used to construct the questionnaires. Some additional aspects need to be taken into account when constructing a questionnaire.

A first decision to be made is the degree of *structure imposed on responses*. In general, there are two kinds of questionnaires, an open-ended (in which the respondents fill out the questions in any order, providing the answers in their own words) and a structured closed-ended (in which possible responses are provided from which the participants must select). Taking into account that we have previously performed a qualitative open-ended interview phase, we already gained a better insight into the various (potential) determinants of board effectiveness. Our aim now is to further elaborate the importance of a selected number of determinants on a more quantitative base as well as to explore how they occur in practice. For that purpose, we opted for two structured closed-ended questionnaires whereby the response category takes the form of rankings. It must be noted that we deliberately opted not to use any form of Likert scales as frequently used in quantitative research. Although Likert scales might offer greater opportunities for statistical analysis, their success depends to a large extent on the quality of the test items or statements (Dillon et.al., 1994). With respect to our research, most of the statements used in the questionnaires were derived from the earlier open-ended interviews and by consequence not sensitive enough to discriminate and thus create variability. The latter is seen as one of the requirements for using Likert scales (Dillon et. al., 1994).

A second aspect relates to the *wording of questions*. In constructing the questionnaires we have explained or tried to avoid words which have different interpretations. In particular, in the beginning of the questionnaires we clearly stated how board effectiveness should be interpreted to limit confusion on the definition of this terminology. Moreover, in order to enhance clarity, we indicated the purpose of the questionnaires and described how the rankings should be interpreted. We have also tried to phrase the questionnaires' items in a neutral, objective and simple way and refrain from using strong adjectives. As a result, we presume that the questionnaires are easy to understand and do not pose a major problem to be completed by high level people, such as directors.

A third aspect concerns the *language*. In order to capture the full spectrum of directors in Belgium and to avoid misunderstanding of the items included, the questionnaires were

drawn up in two languages namely Dutch and French. Translation of the questionnaires to French was done by a native speaker and verified by a third person.

Implementation of the questionnaires. The questionnaires were submitted to the respondents in two steps. First, the respondents were asked to rank the items included in the first questionnaire according to their importance varying from 1 (item is most important) to 10 (item is least important). After a period of time, the respondents received the second questionnaire, but this time they were asked to assign a ranking to the (same) items, indicating to what extent there is room for improvement in practice (ranging from 1 = item needs most improvement to 10 = item needs least improvement).

- Other methods

Other methods have also contributed to the collection of data and to a better understanding of the research topic. During the whole research project national and international conferences, focusing on corporate governance and especially boards of directors, were frequently attended both as a speaker and a participant. In particular, there was an active involvement in the seminars organized by the Belgian Governance Institute. Conferences and seminars are important sources of information. They provide valuable information on new developments in the field, the issues at stake and actors involved. They also offer an important opportunity to meet and discuss with directors in an informal way and as such, to get a better feeling of what is happening within the field. Finally, they can be used to present or confront directors with the results of empirical studies, and consequently, to gather additional comments for further clarification of unexpected findings.

3.3.2.2 Data analysis

The choice to opt for a mixed methods research yields two kinds of data. The empirical data, obtained from the first phase, is qualitative in nature while in the second phase

quantitative data was gathered. Researchers must be aware that the data-analytical methods differ according to the nature of the data. Put differently, qualitative data requires another approach for analysing and interpreting, compared to quantitative data. The analysis of our data set follows the model of Onwuegbuzie and Teddlie (2003). They describe several data analysis stages for mixed methods research: data reduction, data display, data transformation, data integration. These stages are to some extent sequential. In what follows, each stage will be briefly explained and its application to our data sets will be described.

- Data reduction

Data reduction refers to the process of selecting, focusing, simplifying and transforming the raw data which is gathered at the data collection stage. Reducing data, helps to sharpen, sort and organise data in such a way that final conclusions can be drawn and verified (Miles and Huberman, 1994). Both qualitative and quantitative data can be reduced and transformed in many ways.

Qualitative data reduction. In order to reduce the qualitative data, generated from the interviews, we opted for *coding*. Codes are “tags or labels for assigning units of meaning to the descriptive of inferential information compiled during a study” (Miles and Huberman, 1994:56). Codes can be attached to words, phrases, sentences or whole paragraphs. An important feature of coding is that the words themselves do not matter, but instead, their meaning is important. In a first step, we’ve created a provisional “start list” of broadly defined codes. The codes were given names that are close to the concepts they describe. The codes were extracted from different sources such as the literature on boards of directors, insights into the corporate governance codes etc. However, during the coding phase new themes emerged which did not fit into the predefined list, while other codes flourished too much. Too many text segments received the same code. Therefore our start list needed revision by adding new codes and breaking down certain codes into sub codes. The revised list can be found in Appendix 1. Parallel, operational definitions of the codes were foreseen to make sure that the codes were applied consistently over

time. For the process of coding, we have used the software ATLAS.ti. Reducing our qualitative data set by coding, allows for categorizing of the initial data, which permits further clustering of text segments.

Quantitative data reduction. The two small questionnaires provide quantitative data on the determinants of board effectiveness in the form of rankings. Rankings are ordinal data and by consequence not suitable to all kinds of statistical analysis. The numerical data was reduced by computing core descriptive statistics using the software SPSS.

- Data display

Qualitative data display. The main category of displays that have been used with respect to the qualitative data are tables. Tabular displays of information are a means to organize the data and present the groupings of data in a clear way (Miles and Huberman, 1994).

Quantitative data display. Quantitative data is primarily displayed by means of frequency tables.

- Data transformation

In some cases it is appropriate to “quantitize” or “qualitize” the data. Quantitizing simply refers to the process of transforming or converting qualitative data into numerical codes that can be statistically represented and analysed, while qualitzing refers to the opposite process (converting quantitative data into narratives that can be analyzed qualitatively) (Teddlie and Tashakkori, 2003). With respect to our study we decided to use *quantitizing* by introducing a basic form of *counting* in the analysis of the qualitative data. Counting is considered to be a manifestation of the quantitizing process, as described above (Onwuegbuzie and Teddlie, 2003). Miles and Huberman (1994) provide two rationales for counting which are also applicable to our study. First, counting helps to identify patterns more easily. Numbers are by definition more economical and easier to manipulate, compared to words. Counting observations enables one to “see” the data and

often generates more meaning in addition to their narrative descriptions (Sandelowski, 2001). It allows us to more fully describe and/or interpret the variety of criteria related to board effectiveness, which were cited during the interviews. Second, counting helps to maintain analytical integrity. Analysing qualitative data occurs to some extent by insight and intuition. Inherent in this approach is the danger of “overweighting” emerging themes, while ignoring data that does not go in the direction of the researcher’s reasoning (Sandelowski, 2001; Miles and Huberman, 1994). In this respect, computing frequencies during qualitative data analysis is a good way of testing for possible bias and provides a way of increasing legitimation and validity (Onwuegbuzie and Teddlie, 2003). It must be noted that the use of quantitized data in a qualitative study does not change the initial qualitative nature of the study (Morse, 1991). Put differently, when we apply frequency data with the objective of enhancing the description of our interview data, we do not constitute a quantitative study. The main purpose of introducing the counting is to see how robust our insights are.

- Data integration

The final stage in the analysing process is the integration of data. Taken into account the features of our sequential exploratory design, we work with qualitative and quantitative data within two separate sets of coherent frameworks, which in turn lead to the interpretation of the entire data analysis and the formulation of overall conclusions. Table 9 summarizes the data analysis chain for our study.

Table 9: overview of the data analysis activities

<i>Stage</i>	<i>Qualitative data set</i>	<i>Quantitative data set</i>
Data reduction	Coding	Descriptive statistics
Data display	Tables	Tables
Data transformation	‘Quantitizing’ through counting	No transformation
Data integration	Interpretation of the entire analysis and formulation of overall conclusions	

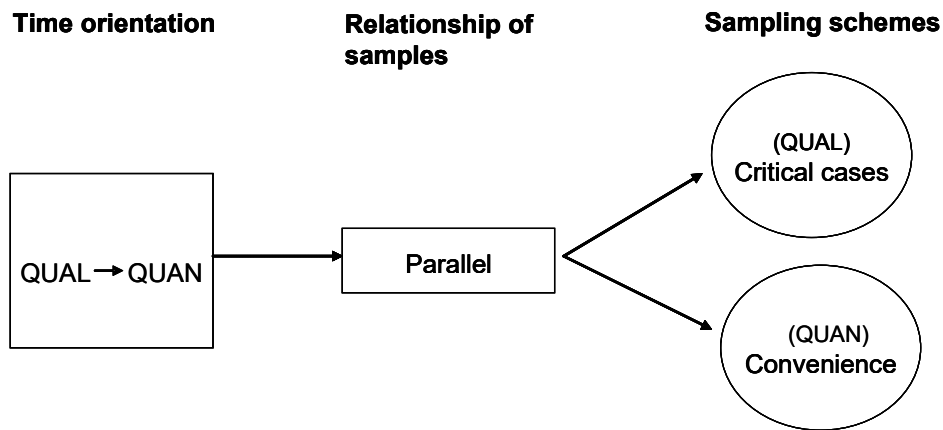
3.3.3 *Legitimation in mixed methods research*

As in any research, attention should be paid to the legitimation and trustworthiness of our findings. In quantitative as well as in qualitative research, legitimation has been operationalized in a myriad of ways, while the nomenclature applied to assess the quality differs between the two types of research (Creswell, 1998). With respect to mixed methods research, the issue of legitimation is still in an embryonic stage (Brannen, 2005; Teddlie and Tashakorri, 2003). However, agreement seems to exist that two important limitations also apply to mixed methods research namely validity (internal and external) and reliability. *Internal validity* with respect to mixed methods research concerns the quality of the inferences that emerge from the quantitative and qualitative data. Inference can be defined as “to bring or carry in; cause; induce or to draw a conclusion as by reasoning” (Teddlie and Tashakorri, 2003:35). *External validity* is the extent to which the findings of the study can be transferred/generalized to other settings, populations, contexts etc. (Teddlie and Tashakorri, 2003). It is argued that the two issues can be addressed simultaneously by paying special attention to the *sampling design* (Collins et.al., 2006). In essence, the choice of research samples should correspond with the applied mixed methods research design, and as such, with the purpose of the study. Put differently, the selected samples should enable us to collect as much robust data as possible, in order to fully understand the phenomenon under investigation (these are the key factors that potentially contribute to board effectiveness). In this respect, rather than selecting a truly random (statistical) sample, it is important to select *information rich cases* from which we can learn most.

In particular, we used the framework of Onwuegbuzie and Collins (in press) to identify a sampling design that fits our research objectives and design. A distinguished feature of this framework is that it provides a two-dimensional typology of available mixed methods sampling models. The first dimension relates to the time orientation of the qualitative and quantitative research phases (sequentially or concurrently). The second dimension is the relationship of the qualitative and quantitative samples. This relationship can be identical, parallel, nested or multilevel. With respect to our study, we have opted

for a *sequential design using parallel samples* for the qualitative and quantitative components of the study. A sequential design denotes that we needed the findings stemming from the sample of the first phase to drive the selection of the sample for the second phase. Parallel samples denote that we use the same underlying population (boards of directors of Belgian companies) from which we draw different samples (directors from listed companies and directors from non-listed companies) (see also Chapter 4). Perhaps more important for assessing the validity threats is the use of *purposeful sampling* (in contrast to probabilistic sampling). In fact, the research samples were selected purposefully utilizing (a) a *critical cases* sampling scheme for the qualitative phase and (b) a *convenience* sampling scheme for the quantitative phase. Figure 10 visualizes our sample design.

Figure 10: two-dimensional mixed method sampling design



Notation: “qual” stands for qualitative, “quan” stands for quantitative, “→” stands for sequential,
 Source : Collins et.al., 2006

As indicated above, purposeful sampling or non-probability sampling implies that we intentionally selected specific respondents that would provide the most information for the first research question. With respect to the sample for the qualitative phase, we have chosen individuals based on specific characteristics because their inclusion provides us with compelling insights into the determinants of board effectiveness. These are referred to as critical cases (Collins et.al., 2006). More specifically, we have selected members of the boards of directors of Belgian listed companies including different directors’ roles

such as chairmen, independent directors, non-independent (dependent) directors and CEOs. With respect to the sample for the quantitative phase, we have chosen individuals that are conveniently available and willing to participate in the study (Collins et.al., 2006). The rationale for this choice is the awareness of the difficulties to obtain access to boards of directors and to board members. Accessibility is even more uncommon regarding boards of directors of non-listed companies. Therefore, we have made an appeal to the member network of the Belgian Governance Institute to distribute the questionnaires we are using in the quantitative phase. The Belgian Governance Institute represents 715 members⁵ mainly including directors and, to a more limited extent, other actors in the field of corporate governance (advisors, academics, lawyers etc.).

Finally, *reliability* refers to the extent to which the study can be replicated by different researchers, producing the same results (Carmines and Zeller, 1979). Regarding the issue of reliability, it is important to clarify how the study has been conducted, which data has been gathered and how the data has been interpreted. These points have already been described in the previous section concerning the methods.

3.4 Research strategy and methods associated with the second part of the research project

3.4.1 Research strategy: a case study

3.4.1.1 Definition

The research strategy adopted for the second part of the research project is *a case study*. A case study is an empirical enquiry that investigates a contemporary phenomenon within its real-life context, especially when the boundaries between phenomenon and context are not clearly evident (Yin, 2003). Unlike an experiment, which isolates the phenomenon

⁵ This number reflects the size of the member network at the time this study was done.

from its context, a case study strategy targets capturing the interconnectedness of the phenomenon and its context. The case study is a way of obtaining detailed, comprehensive, systematic and in-depth information on real-life events. Conducting a case study also means relying on several ways to gather and construct empirical material, as well as meeting with several actors (Yin, 1994). In particular when using interviews, like we do in this research project, a case study involves letting many voices be heard, i.e. to talk to many different actors with different relations to and positions in the case under study.

3.4.1.2 Motivation for the case study strategy

Although many possible research strategies might be appropriate to address the second research question, several reasons support the choice for a case study approach. A first criterion is the *nature of the research question*. Continuing on the findings of the first part of the research, whereby we have explored the variety of factors and their importance for board effectiveness, the second part of the research intends to discover the relationships between the different factors. In particular, we try to explain how the different factors interrelate, influence each other and contribute to the effectiveness of boards of directors. As such, the research concerns a ‘how’ type of question. According to Yin (2003), the use of case studies is the preferred research strategy when dealing with ‘how’ questions which are more explanatory. Second, of importance for choosing a case study research is the *need to further develop theory*. Emory and Cooper (1991) state that “a single, well-designed case study can provide a major challenge to a theory and provide a source of new hypotheses and constructs at the same time” (p.143). The results can not only falsify hypotheses or assumed relationships but also provide new insights into the theory. In this respect, case study research can be inductive (developing a theory through inductive and qualitative study of the phenomenon (Eisenhardt, 1989) or deductive (starting from a theoretical model and testing hypotheses (Emory and Cooper, 1991). We follow the deductive research approach. Based on the exploratory field study, we have developed a theoretical research framework for board effectiveness and, supported by literature, have

identified relationships amongst the selected variables (we refer to Chapter 5 for a description of the research framework). A case study strategy will allow us to make these relationships stronger. It is argued that such a strategy can be very powerful for explaining relationships or causality between variables. As noted by Miles and Huberman (1994) a case study can provide a close look, which can identify mechanisms going beyond sheer associations. It also offers the possibility to deal with the complex network of processes in real life situations. A third characteristic is the *focus* of the research on *contemporary* rather than historical *events*, as we analyse the actual working of the board of directors. Although boards of directors have been investigated for years, the interest for corporate boards has dramatically increased during the corporate governance era, a phenomenon that has substantially grown over the past two decades. So its history is very recent. This contemporary aspect of the research requires interviewing the persons involved in the recent events. In this respect, a case study is well-suited, when examining contemporary events (Yin, 2003). Finally, our research also tries to get a better *insight* into the *more intangible aspects* of board effectiveness. These aspects are rather difficult to discover, using quantitative research approaches. Moreover, they have, at this moment, rarely been investigated because directors or boardrooms are often not accessible. According to Hartley (1994) case studies can be tailor-made to explore behaviour or processes which are little understood. The case study offers the opportunity to go into the details, which allows the examination of specific issues in considerable depth. It is of great value to understand processes at a micro level. Moreover, it provides practical insight, which enhances our understanding of intangible aspects or group processes and the extent to which they influence board effectiveness.

3.4.1.3 Case study designs

Case study research can have different designs including single or multiple-case studies (Yin, 1994). For the purpose of our research we have opted for a **single case study design**. The major rationale for the choice of a single case study is the fact that it represents the *critical* case in validating or testing a clear set of propositions derived from

theory (Yin, 2003). The case will be used to determine whether the propositions, as defined in our theoretical research framework, are correct or whether some alternative set of explanations might be more relevant. In this respect, Stake (2005) uses the term instrumental case study indicating that it is not the case itself that is of interest but that a particular case is examined mainly to provide insight into an 'external' issue of interest. The case itself plays a supportive role as it facilitates our understanding of something else, which is the base for theorizing of a phenomenon. Moreover, a single case study design works effectively to investigate a phenomenon previously inaccessible to scientific investigation. Put differently, the opportunity to learn is important when conducting a case study (Stake, 2000). As noted previously, boards of directors have largely been shielded from view, and accessibility to boardrooms and board members is very difficult. As a result, board research has traditionally been conducted from a distance, using quantitative research techniques and secondary data sources. We were offered the opportunity to study the board of directors of a large Belgian listed company, in close interaction with all board members, and as such, to examine the phenomenon of board effectiveness in a real-life context.

3.4.1.4 Common prejudices against case study research and the actions taken

Although the advantages of using case studies are numerous, this kind of inquiry is not without limitations and problems. Two important limitations are frequently raised with respect to case studies: validity and reliability. More specifically, Yin (2003) has identified four problems which have been taken into account during the execution of the case study: (i) construct validity or the establishment of correct operational measures for the concepts being studied; (ii) internal validity or the establishment of causal relationship, whereby certain conditions are shown to lead to other conditions, as distinguished from spurious relationships; (iii) external validity or the establishment of the domain to which a study's findings can be generalized and (iv) reliability or the demonstration that the operations of a study can be repeated, with the same results.

In order to limit the problems associated with **construct validity**, we applied several tactics as suggested by Yin (2003). During the case study, we've used multiple sources of evidence such as interviews, a written questionnaire and documentation. This way of collecting data helps to overcome the limitations of each source but, above all, encourages what Yin (2003) calls "convergent lines of inquiry" (p.36). The multiple sources of evidence provide multiple measures of the same phenomenon, allow more accurate findings and hence increase construct validity. The second tactic is the creation of a chain of evidence. According to Yin (2003) this "allows an external observer to follow the derivation of any evidence, ranging from initial research questions to ultimate case study conclusions" (p.105). The purpose is to trace the steps between the beginning and the end of the case study, and backwards. In order to allow the reader to do so, we've included the circumstances under which the data has been gathered, such as the time and place of the interviews. Both the questionnaire and interviews were based on questions and constructs, derived from the theoretical framework. In this respect, a clear link exists between the empirical data and the theory. The final tactic, that helps to diminish the problem of construct validity, is the presentation of (a first version) the case study report to the Remuneration and Compensations Committee of the case under study. The other board members also received a copy of the written report in order to check the truthfulness and accuracy of the information reported. They were asked to send comments back to the author(s). Besides, the report of each interview has also been reviewed by the other members of the interview team, including the Company Secretary.

The second problem relates to **internal validity**, because we used the case study for explanatory purposes. As we are trying to determine whether input X leads to outcome Y, there is a danger to incorrectly conclude that there is a causal relationship while ignoring a potential third factor Z which actually might have caused Y. The technique we used to deal with the internal validity of our case study is pattern matching and in particular the use of rival explanations as a pattern, as suggested by Yin (2003). On top of that, we also make use of investigator triangulation (we refer to paragraph 3.4.2.4 for a more detailed description of these techniques).

The third problem, **external validity** has been frequently criticised in case study research. The critique concerns the limited ability to generalize the case study findings to a larger population. Generalizing means taking results and conclusions beyond the particular context in which they were generated. Typically, when assessing the generalization of findings from a particular research, special attention is paid to the extent to which the results can be said to be valid for the whole population from which the sample in a study is drawn. This is the conventional notion of statistical generalization. Most often, however, qualitative research conducted towards reaching a rich understanding through in-depth studies of a small number of cases is considered a poor base for such (statistical) generalization. Although this critique is justified, the problem boils down to the notion of generalizing. Yin (2003) notes that case studies are a good base for generalizing to theoretical propositions, rather than populations or universes. This type of generalization is referred to as *analytical* or *theoretical* generalization (in contrast to statistical generalization). For that purpose, he advises to use theory when conducting a single case study. In essence, before analyzing and carrying out the case study we developed a research framework which makes use of existing theories to derive theoretical propositions. In addition, we compared conflicting findings with a broad range of literature in order to elaborate our theoretical model. Further, we also include literature discussing similar findings, either in board research or in different contexts. As such, tying emergent findings to existing literature enhances not only the internal validity (see previous paragraph) but also the generalizability (Eisenhardt, 1989).

In order to solve the last point, **reliability**, Yin (2003) proposes to use a case study protocol and to develop a case study database. The *case study protocol* is a written document, including a brief explanation of the research purpose, a list of questions for the interviews, detailed information on the appointment with the board members, an overview of other data sources etc. (see Appendix 2). The *case study database* is a way to store and organize all the materials collected and/or used during the case study. A formal case study database has the advantage that raw data can be retrieved at any moment in time both by the investigators and by other persons. The majority of the case study materials takes the form of computerized data files which are electronically classified.

Other documents (e.g. field notes) are stored in a separate library. Furthermore the chain of evidence, explained in the previous paragraph, also benefits the reliability of the information in the case study.

3.4.2 Methods

3.4.2.1 The single case study

For the second part of the research, the field study consists of a single case study. The case under study is a recently listed company and Belgium's largest telecom operator. At the moment of the case study, the Company is controlled by a majority shareholder, holding more than 50% of the shares. The shareholder structure - in the meaning of block holdings - is very similar to many listed companies in Belgium (see Chapter 2).

In line with the discussion in paragraph 3.4.1.3, this particular company was chosen for the case study for two reasons. For the first time in years, we were presented with the opportunity to gain access to the full board of directors of one of the largest listed companies in Belgium. We were allowed to probe all the directors as part of a board evaluation project. As a consequence, we seized the opportunity to combine the project with a case study research. Although we were not able to observe the directors inside the boardroom, interrogating all directors of the same board enhances the understanding of how a board operates and how its effectiveness is perceived by its members. Moreover, it enables one to explore the relationships and connections amongst the complex web of factors that contribute or hinder the effectiveness of a board. Second, due to several forces, the Company and its board of directors have been subject to some major changes. For example, the recent IPO triggered a change in the governance structure and the board of directors has been adjusted according to the recommendations of the Belgian Corporate Governance Code. Moreover, the IPO as well as the high-velocity environment the Company is operating in, undeniably have an impact on the role the board is expected to perform (see Chapter 6). In this respect, the board of directors is relatively 'new' and

well-suited (i) to explore the impact of specific board attributes (e.g. independent directors) which are assumed to be important corporate governance mechanisms for board effectiveness, and (ii) to discover the impact of the context on the effectiveness of boards.

3.4.2.2 Multiple sources of evidence

During the case study, empirical data was collected using three main sources of evidence: interviews, a written questionnaire and documentation. Each source has its strengths and limitations but used together in a single study, they augment the evidence and make the findings more robust. We have already touched upon the strengths and weaknesses of interviews and questionnaires in paragraph 3.3.2.1 as these techniques have also been used in the first part of the research project. In addition, Table 10 provides an overview of the strengths and weaknesses of documents. The three sources of evidence used in the case study are presented in the following paragraphs.

Table 10: strengths and weaknesses of documentation as a source of evidence

<i>Research Technique</i>	<i>Strengths</i>	<i>Weaknesses</i>
Documentation	Stable – can be reviewed repeatedly Unobtrusive – not created as a result of the case study Exact – contains exact names, references, and details of an event Broad coverage – long time span, many events and many settings	Retrievability – can be low May be incomplete because of selective reporting Reporting bias - reflects (unknown) bias of author Access – may be deliberately blocked

(Sources: Yin, 2003; Johnson and Turner, 2003)

- Questionnaire

The first main technique used in the case study is a written questionnaire. As described in paragraph 3.3.2.1 a questionnaire is a self report instrument that research participants are expected to fill out (Johnson and Turner, 2003). All 17 members of the board of directors filled out the questionnaire before the start of the interviews.

Construction of the questionnaire. The written questionnaire is the result of a continuous interaction between the researcher and the Company. This interaction was necessary for the sake of completeness. After all, the instrument must meet the requirements of the case study as well as serving the particular objectives of the board evaluation project. Consequently, the questionnaire covers a broad range of issues that are of relevance to both parties. As previously explained (see paragraph 3.3.2.1), some additional aspects need to be considered in constructing a questionnaire.

The first decision to be made is the degree of *structure imposed on responses*. For the purpose of the case study we used a quantitative questionnaire which is based on completely structured and close-ended questions (Johnson and Turner, 2003). This means that possible responses are provided and the respondents are ‘forced’ to select from the pre-selected alternatives. The advantages of this kind of questionnaire are its efficiency and reliability (Fink and Kosecoff, 1985). It is efficient because it is simple for the respondent to use while easy for the researcher to code for computer analysis. The increased reliability stems from the uniformity of the data this kind of questionnaire provides, because each respondent answers the same questions with the same options (e.g. agree or disagree). Close-ended questions are also preferable in larger questionnaires. Moreover, we used 5-point Likert scales for all the questions. A Likert scale is a bipolar scaling method, measuring either a positive or negative response to a statement. In particular, the directors were asked to specify their level of agreement to each item on a list of statements. The latter was ordered amongst eight themes and after each theme some open space was foreseen with the objective to allow the directors to write down any comment or suggestion.

Another aspect concerns the *language*. In order to minimize potential biases in the responses -due to the different national languages-, the questionnaire is written in English.

We did not formally *pre-test* the questionnaire due to three reasons. First, the case study questionnaire is to a large extent based on existing questionnaires that have been used in prior research on corporate governance, and as such, have per definition been pre-tested before. Second, the questionnaire has been screened and obscurities slightly adapted. Third, regarding specific constructs related to our theoretical framework, commonly used scales were extracted from the literature and included in our questionnaire. Finally, the questionnaire was formally approved by the Remuneration and Nomination Committee of the Company, before sending it out to the other board members.

Implementation of the questionnaire. The questionnaire was sent to the board members by mail. The cover letter was personalized, introducing the purpose of the questionnaire and informing the directors about the next steps in the process. In particular, the directors were asked to fill out the questionnaire before the interview took place. In sum, the mail-out package consisted of a cover letter, the questionnaire and a self-addressed, stamped return envelope.

- Interviews

The second main technique that is used for data collection is interviewing. According to Denzin and Lincoln (2005) the interview is “a conversation – the art of asking questions and listening” (p.643) (see also paragraph 3.3.2.1 for more information on the technique of interviewing). The members of the board of directors were individually interviewed in a face-to-face verbal interchange (in the directors’ mother-tongue). The two foreign directors were individually interviewed by telephone. The interview typically lasted for one to one and a half hours, but occasionally took as long as three hours.

Type of interview. As described in paragraph 3.3.2.1 there are many different types of interviews, depending on the purpose of the interview. For the case study, we agreed to use *focused* interviews. Focused interviews are - to some extent - of an open-ended nature and assume a conversational manner, but in fact the investigators follow a certain set of questions derived from the case study protocol (Yin, 2003). These questions are linked to

our theoretical framework, reflect our actual line of inquiry and are developed following the guidelines of Yin (2003). Regarding data collection, he distinguishes two levels at which the questions can occur. Level 1 relates to the questions asked to the board members and reflects the *verbal* line of inquiry. Level 2 relates to the questions asked in relation to the individual case and these questions are posed to the investigator. They reflect the *mental* line of inquiry⁶. Relying on this format, we were able to put forward the same questions in the same way to all the board members although the sequence could vary. Next to the predefined questions, additional questions were posed in order to get some clarification of specific answers or comments in the written questionnaire.

Interview team. A critical issue in doing interviews is the possible impact the interviewer has on the interviewee and by consequence on the quality of the collected data. It is important that the interviewer(s) generate(s) trust and respect to convince the interviewee that the interview is being done for a good cause and the assurance of confidentiality is legitimate (Fontana and Frey, 2005). Besides, the interviewer(s) should appear familiar with the topic under investigation, expose professionalism and/or occupy a role of authority in the field (Fowler and Mangione, 1990). To address these two crucial aspects, special care was taken of the composition of the interview team and it was decided to compose the interview team of both an outsider (the researcher) and an insider (the Company Secretary).

No audiotapes. It was decided not to tape-record the interviews for three reasons. First, we believed that the presence of a tape-recorder could influence the behaviour of both the interviewee (because he/she does not like to be tape-recorded) and the interviewers (because they are unfamiliar with the technique). Second, during the interview some sensitive topics were tackled and tape-recording could be inconvenient to freely speak up and utter one's opinion on the topic. Third, the absence of a tape-recorder could reinforce our guarantee of anonymity of individual responses. The disadvantage of not using audiotapes is the increased chance of bias and inaccuracy in interpreting the answers. In

⁶ The comparison with a detective can clarify the difference between the two levels. The detective has in mind what the course of events in a crime might have been (Level 2) but the actual questions posed to any witness or suspect (Level 1) do not necessarily betray the detective's thinking.

paragraph 3.3.2.1 we already touched upon the different actions that can be taken to reduce this problem. First, we respected the "24 hour" rule which requires that detailed interview notes and impressions be completed within one day of the interview (Eisenhardt and Bourgeois, 1988). During the interviews detailed field notes were taken and electronically transcribed in a computer document immediately after the interview took place. If there was any doubt on the interpretation or meaning of specific responses, the latter was discussed more in-depth with the other team members. Individual records were then sent to the other member(s) of the interview team in order to check the information. Second, the field notes included all data, regardless of their apparent importance at the interview, completed with our ongoing impressions (Eisenhardt and Bourgeois, 1988). Third, each member of the interview team received a written script of the main interview questions in order to standardize to some extent the interview procedures. Finally, there was a mutual monitoring of the interviewers to get the most accurate data possible (Fink and Kosecoff, 1985).

3.4.2.3 Documentation

For case studies, documentation is very relevant, but Yin (2003) noted that it must be used with care and should not be accepted as a literal recording of events that have taken place. In other words, most documents are made for purposes other than the case study and might be deliberately edited or biased by the author. Still, they can offer a rich source of insights into the participants' interpretations of organisational life. The main purpose of using documents in this case study was to corroborate and augment evidence from other sources and to supplement other sources of information. Documentation comes in many forms, but in general, two types of documents can be distinguished: primary and secondary documents. Primary sources are materials that are gathered first hand and which have a direct relationship with the people, situations or events under study. Secondary sources are materials that are published. Both types of documents have been collected and used for the purpose of our research (Table 11 presents an overview).

Table 11: documents used in the case study

<i>Source</i>	<i>Type of documents</i>
Organizational documents	
Primary documents	Summary of the chairman's introductory discussions with the individual directors Briefing notes
Secondary documents	The company's Articles of Association The company's annual reports Corporate governance charters Press releases
Other secondary documents	Law 21 March 1991 and the Company Law The company's website Summary of an analysis on the company's Corporate Governance Structure by a legal advisor in February 2005 Newspaper cuttings

3.4.2.4 Data analysis

The empirical data collected during the interviews is qualitative in nature. In order to capture the essence of this data, validation and verification methods are necessary. To analyze the qualitative data we follow the approach put forward by Miles and Huberman (1994). They substantiate that analysis consists of three concurrent flows of activity: data reduction, data display, and conclusion drawing/verification. These three activities can be interwoven before, during and after the data collection. In what follows, we briefly describe each activity and explain how they are applied in our study.

- Data reduction

As explained in paragraph 3.3.2.2, data reduction refers to the process of selecting, focusing, simplifying and transforming the raw data of the field notes. Data reduction already starts at the stage of data collection. By deciding which case to study, which approaches to use for the collection of the data, there is already some kind of data

reduction. Reducing the large amount of available data helps to focus on the most relevant issues in such a way that final conclusions can be drawn and verified. Data reduction does not mean, per definition, quantification. In fact, qualitative data can be reduced and transformed in many ways.

In order to reduce the data, we relied on the theoretical research framework which we have developed in Chapter 5. This framework offers an analytical tool that allowed us to develop a chain of questions, from the theoretical to the operational level. It has been used to operationalise the theoretical questions, in order to enable their investigation, and to refer to when analyzing the data. In essence, the various constructs and potential relationships amongst these constructs, derived from the theoretical research framework, were used as a guideline to order and summarize the available data. We used *pattern coding* as a way of grouping summaries into a smaller number of sets, themes and constructs. (Miles and Huberman, 1994). Pattern codes are defined as “explanatory or inferential codes, ones that identify an emergent theme, configuration or explanation. They pull together a lot of material into more meaningful and parsimonious units of analysis” (Miles and Huberman, 1994:69). This technique helps to channel the data in order to discover common themes amongst the respondents, to reveal causes/explanations and to allow new elements to surface.

- Data display

Data display refers to the techniques that are used to organize and/or to visualize the information in an accessible and compact form. The main technique that is used regarding the analysis of the case study is matrices. Matrices involve the crossing of two or more main dimensions or variables to see how they interact (Miles and Huberman, 1984). Matrices come in many forms and there are no fixed rules for constructing a matrix. In essence, matrix construction depends on one’s understanding of the substance and meaning of the database. The issue is not to construct ‘right’ matrices but whether the matrices are helpful to provide answers to the questions at stake. In this respect, we

developed matrices which enable us to compare the data of all respondents for a certain theme.

- Conclusion drawing

Drawing conclusions refers to the way meaning is given to the collected information. It implies noting regularities, patterns, explanations etc. As explained in paragraph 3.4.1.3, the case study is used for explanatory reasons. The purpose is to examine to what extent our theoretical research framework is valid by verifying the propositions derived from theoretical assumptions. Essentially, we draw conclusions based on two analytical techniques (i) triangulation and (ii) pattern matching.

In general, the term **triangulation** refers to the combination of qualitative and quantitative methods to address the same research problem (Jick, 1979). The rationale is that multiple and independent measures, if they reach the same conclusions, provide a more certain portrayal of the phenomenon under study. As such, the technique of triangulation can be used to cross-validate or confirm findings within a single study (Greene et. al., 1989). In our case study we used two types of triangulation. First, we used *data triangulation* or multiple sources of evidence. These are qualitative interviews, a written questionnaire and company documents. These data sources are expected to complement each other and they provided us with qualitative and quantitative evidence which we combined to draw conclusions. Both data types are highly synergistic, as qualitative data is useful to understand the evidence emerging from the quantitative sources. Conversely, the quantitative data is useful to corroborate those findings from qualitative evidence (Eisenhardt, 1989). Second, we respected the technique of *investigator triangulation* or the use of multiple investigators. In our research, the case study respondents (interviewees) were interviewed by a team (of 2 or 3 interviewers), which is a common strategy recognized for employing multiple investigators (Eisenhardt, 1989). Moreover, we used a tactic of giving the team members a unique role, where one or two researchers handled the interview questions while the other records notes and observations (Eisenhardt and Bourgeois, 1988). The technique of investigator

triangulation allows the data to be observed from different perspectives. These complementary insights enhance the creative potential of the data as well as the likelihood of capitalizing on any new insight that emerges from the data. Moreover, the convergence of observations and perceptions from multiple investigators increases the confidence in the findings.

Pattern matching is a logic which compares an empirical base pattern with a predicted one and it is considered to be one of the most desirable techniques for case study analysis (Yin, 2003). In our case study we applied the *technique of rival explanations* to account for findings with respect to the independent variables. While the theoretical research framework provides predefined propositions in terms of inputs (independent variables) and outcomes (dependent variables), there is still the possibility that the empirical findings do not match with the predicted relationship. Successful matching of the empirical pattern to a rival explanation provides the base for concluding that this explanation is the correct one (and that the initial predicted one was incorrect) (Yin, 2003). Besides, the technique of rival explanations is also of added value for theory building as we consider it as a tool for identifying shortcomings in our theoretical framework. In particular, we compared emerging unexpected relationships with literature in order to understand to what extent it contradicts and why. Examining literature to explain conflicts with the predefined propositions, is considered to be an essential feature of theory building for two reasons. First, the confidence in the findings may be reduced when conflicting findings are ignored. Second, the juxtaposition of conflicting results forces one to consult a broad range of literature which offers an opportunity to exhibit a creative, frame breaking mode of thinking (Eisenhardt, 1989).

3.5 Conclusion

The chapter on methodological considerations has presented the choices involved in carrying out the present study. Although our research project can be divided into different parts with implications for the research strategy and methods used, we have documented

in detail that a coordinated qualitative methodology is selected because it is assumed to be the most appropriate way to investigate the phenomenon of board effectiveness. In essence, we believe this methodology enables a better understanding of ‘what’ determines the effectiveness of boards as well as ‘how’ effectiveness is shaped by a complex web of interrelated factors. Moreover, we are convinced that qualitative research provides a valuable counterbalance for the large amount of quantitative studies commonly found in board research.

As with any research methodology, the qualitative approach has some limitations, in particular concerning the subjectivity issue. Although the latter can not be completely avoided, a number of measures have been taken in order to limit this problem as much as possible. Special attention was paid to selecting the most appropriate research strategy and methods that fit with the issues under investigation. In this respect, we opted for a mixed methods research for the first part of our study and a case study for the second part. In both cases, we combined multiple data techniques, such as interviews and questionnaires, which yielded qualitative and quantitative evidence in order to elaborate or corroborate the findings.

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4 Identifying key determinants of effective boards of directors

4.1 Introduction

As pointed out in Chapter 2, boards of directors are of interest to academics, the investment community, the business world and society at large. According to Cadbury (1999) this attention is understandable, given the fact that boards of directors serve as a bridge between the shareholders, who provide capital, and management in charge of running the company. At the heart of the corporate governance debate is the view that the board of directors is the guardian of shareholders' interest (Dalton et.al., 1998). Yet, boards are being criticized for failing to meet their governance responsibilities. Major institutional investors put pressure on (incompetent) directors and have long advocated changes in the board structure (Monks and Minow, 2001). Their call has been strengthened by many corporate governance reforms resulting from major corporate failures. The reforms put great emphasis on formal issues such as board independence, board leadership structure, board size and committees (Weil, Gotshal and Manges, 2002; Van den Berghe and De Ridder, 1999). These structural measures are assumed to be important means to enhance the power of the board, protect shareholders' interest, and hence, increase shareholder wealth (Becht et.al., 2002; Westphal, 1998).

The interest of the investment and business community in the effectiveness of corporate boards undeniable stimulated academic research. Empirical studies on boards of directors are to a large extent triggered by a common question, i.e. whether boards of directors have an impact on corporate performance. Early research on US boards showed a sad picture as it concluded that boards of directors are rather passive, dominated by management and their impact is in fact minimal (Lorsch and MacIver, 1989; Drucker, 1974; Mace, 1971). From a different angle, an extensive body of research has examined the direct impact of board attributes on firm performance. By using a firm's financial performance as a proxy, scholars have been able to empirically test a board's

effectiveness in protecting shareholders' interests. Most of these studies have, however, shown inconclusive results (see the reviews by Coles et.al., 2001 and Dalton et.al., 1998). Another stream of research has investigated the influence of board attributes on the performance of board roles, suggesting an indirect causal relationship between boards of directors and company performance (see the reviews by Deutch, 2005 and Johnson et.al., 1996). A common feature of all these studies is the focus on a limited number of characteristics related to board composition namely insider/outsider representation, board size and CEO duality. This comes as no surprise as (i) their importance is recognized by the various theoretical perspectives on board research (Zahra and Pearce, 1989), (ii) they are common targets of those who seek to reform the corporate governance processes (Dalton et.al., 1998), and (iii) a vast majority of these studies relies on archival data gathering techniques and structural board measures provide the relative ease of data collection (Daily et.al., 2003) (see also Chapter 3).

Notwithstanding the fact that market parties (investors, corporate governance activists etc.) and scholars attach great importance to the same board issues, there are few definitive and striking findings to link these structural board characteristics to performance outcomes (Daily et.al., 2003). Due to the lack of clear and solid academic evidence, the appropriateness of these board measures as adequate proxies for understanding board effectiveness can be questioned. Almost two decades ago, Zahra and Pearce (1989) already argued that there is "a growing awareness of the need to understand better how boards can improve their effectiveness as instruments of corporate governance (...). The starting point for future research involves conducting extensive field work to understand better, document and operationalize board variables. More descriptive work is necessary before normative board models or theories can be advanced" (p.327). Some scholars have tried to overcome the limitations in mainstream board research by examining the explanatory value of individual director characteristics (van der Walt and Ingley, 2003; Kesner, 1988; Vance, 1978), board working style (Gabrielsson and Winlund, 2000) and board processes (Cornforth, 2001) for the effectiveness of boards. In addition, recent qualitative research into boards of directors (Leblanc and Gillies, 2005; Roberts et.al., 2005; Huse et.al., 2005) as well as more

practitioner literature (e.g. Charan, 2005; Carter and Lorsch, 2004; Sonnenfeld, 2002) have brought the importance of studying boardroom dynamics to researchers' attention. Unfortunately the conduct of extensive field work (as called upon by Zahra and Pearce (1989)) remains limited, not in the least because of difficulties of gaining access to boardrooms and directors. Hence, a sufficient insight into the complex web of criteria which enables (or hampers) boards of directors to be effective in conducting their roles and ultimately creating shareholder wealth is - to a large extent - still lacking (Leblanc and Gillies, 2005).

The purpose of this chapter is to try to fill this void as much as possible, by identifying and exploring the broad variety of criteria that may influence board effectiveness. In particular, this chapter addresses the following research question: *What are the key factors that contribute to the effectiveness of boards of directors?* (see Chapter 1). We will investigate this question by means of a mixed methods research design, involving boards of directors of both listed and non-listed Belgian companies as well as other actors in the field. Particularly, we will explore a set of qualitative and quantitative data generated from a sample of directors, who express their views on the criteria of board effectiveness, based on their own (board) experience.

The chapter is organized in four sections. First, we outline the theoretical background. The second section contains an explanation of the research methodology, focusing on the mixed methods research design. The third section presents the results of our study. We end this chapter by discussing our findings and drawing conclusions.

4.2 Theoretical background

In studying boards of directors, academic research has been concerned with mainly three board characteristics: composition, leadership structure and size. They are commonly identified by the basic theoretical perspectives on boards of directors and by consequence

assumed to be important proxies for understanding board effectiveness (Zahra and Pearce, 1989).

- **Board composition as key determinant**

The bulk of academic research on boards of directors examines the role and the proportion of inside, outside and independent directors. In essence, two theories prevail to explain the reliance either on insider or outsider-dominated boards (see also Chapter 2). As previously pointed out, *agency theory* is concerned with conflicts of interest that may occur between the shareholders (principals) and the managers (agents). Separation of ownership and control provides the potential for managers to pursue actions which maximise their self-interest at the expense of the shareholders. The board of directors serves as an internal control mechanism in order to monitor management and to ensure shareholders' welfare (Fama and Jensen, 1983a; Jensen and Meckling, 1976). In an agency perspective, effectiveness is presumed to be a function of board independence from management. Applied to the composition of the board of directors, agency theory prescribes a preponderance of independent outside directors. The opposite perspective is grounded in *stewardship theory*, which perceives managers as good stewards of the company assets. Managers have a range of non-financial motives, such as the intrinsic satisfaction of successful performance, the need for achievement and recognition etc., which restrains them from misappropriating corporate resources at all costs. Reallocation of control from shareholders to management leads to maximization of corporate profits and hence shareholder returns (Muth and Donaldson 1998). Based on these assumptions, stewardship theory suggests a board of directors dominated by insiders. The empirical findings of academic research on board composition, however, do not reveal a consistent picture.

First, a rich body of literature has investigated *the direct impact of board composition on corporate financial performance*, but yielded mixed results. Several researchers have studied the effects of outsider-dominated boards on shareholder wealth and have found positive results. For example, Baysinger and Butler (1985) reported that firms with higher

proportions of independent directors ended up with superior performance records (as measured by return on equity). Rosenstein and Wyatt (1997) found that a clearly identifiable announcement of the appointment of an outside director leads to positive effects on the firm's share price. In contrast, there is also a series of studies that do not support the postulated positive relationship. Agrawal and Knoeber (2001) as well as Coles et.al. (2001) reported a negative impact of greater representation of outside directors on firm performance, as measured by Tobin's Q respectively Market Value Added. In addition, Kesner's findings (1987) indicate a positive association between the proportion of inside directors and two indicators of firm financial performance, profit margin and return on assets. Still others are more reserved on the effects of board composition on corporate performance. Wagner et. al. (1998) conclude that both greater insider and outsider representation can have a positive impact on performance, while a meta-analysis by Dalton et.al. (1998) demonstrates that there is virtually no substantive relationship between board composition and financial performance.

Another stream of empirical research suggests that *board composition is related to the board's undertaking of its roles*, but again the results are mixed. A fair amount of evidence supports the assumption that outside directors have been effective in monitoring management and protecting shareholder interests. Outsider-dominated boards are significantly more likely to replace an underperforming CEO (Weisbach, 1988), to prevent management from paying greenmail (Kosnik, 1987), are more involved in restructuring decisions (Johnson et. al., 1993), and are better able to distinguish between good and bad acquisitions (Byrd and Hickman, 1992). In contrast, some researchers do not support the notion that independent directors are effective guardians of shareholders' interest. For instance, no significant relationship was found between the proportion of independent directors and the adoption of a poison pill provision (Mallette and Fowler, 1992) or the number of illegal acts committed by management (Kesner et.al., 1986). Moreover, some results are rather in favour of insider-dominated boards. Research shows that the proportion of inside directors has a positive impact on R&D spending (Baysinger et.al., 1991), innovation and diversification strategies (Hill and Snell, 1988) and is

negatively associated with the incidence of golden parachute agreements (Cochran et. al., 1985).

- **Board leadership structure as key determinant**

Board leadership structure refers to whether or not there are separate persons who serve in the roles of CEO and chairman of the board. Agency theory, as well as stewardship theory, are also relevant to explain the leadership structure of boards. In an *agency perspective*, the separation of the roles of CEO and chairman of the board is prescribed as a measure for more independent oversight. Splitting these roles dilutes the power of the CEO, avoids CEO entrenchment and reduces the potential for management to dominate the board. A separate board leadership structure provides the required check and balances, and hence, may positively influence company performance (Zahra and Pearce, 1989). This view runs counter to other thinking about CEO duality. In fact, proponents of *stewardship theory* suggest that if the CEO also serves as the chairman, this duality provides unified firm leadership, builds trust and stimulates the motivation to perform. In this perspective, joint leadership structure facilitates better firm performance (see e.g. Muth and Donaldson, 1998; Finkelstein and D'Avanti, 1994). Empirical research on board leadership structure is rather limited and provides inconclusive results supporting, both perspectives.

Only a limited number of studies has empirically examined *the effects of CEO duality on firm performance*. Donaldson and Davis (1991) as well as Coles et al. (2001) reported a positive relationship between a combined leadership structure and shareholder returns, as measured by return on equity, and economic value added respectively. In contrast, Rechner and Dalton (1991) found that firms with separate board leadership structures outperformed - over a six-year time period - those relying upon a joint structure. However, a small amount of studies show no relationship between board leadership structure and firm performance (e.g. Dalton et.al., 1998, Baliga et al., 1996; Chaganti et.al., 1985).

Another way of approaching this issue is by studying *the joint effect of board leadership structure and board composition*. In this respect a robust interaction effect is suggested between firm bankruptcy and board structure. Firms that combine the CEO and chairman roles and that have lower representation of independent directors are associated with bankruptcy (Daily and Dalton, 1994a; Daily and Dalton, 1994b).

- **Board size as key determinant**

Board size is a well-studied board characteristic for two different reasons. First, *the size of the board is believed to have an impact on firm performance*. In particular, in accordance with *agency theory*, the number of directors frequently serves as an indicator of CEO domination of the board. Increasing the number of directors makes it more difficult for the CEO to dominate the board and hence enables the board to better monitor management and corporate performance (Zahra and Pearce, 1989). In addition, the importance of board size is also recognized by *resource dependency theory* (see also Chapter 2). The central postulate of this theory is that external parties hold resources which a business organization perceives as crucial for the realization of its internal objectives (Pfeffer and Salancik, 1978). In order to acquire and maintain these resources, a company seeks to establish links with its environment and the board of directors is a vehicle to do so. According to this perspective, a larger board of directors is presumed to be more capable of co-opting external influences, thus obtaining valuable resources that are inevitable for corporate success (Johnson et.al., 1996). Based on these assumptions, a positive association between board size and corporate performance became conventional wisdom, however the evidence of empirical research on this issue is rather inconsistent. Some early studies provide positive evidence for varying industries. According to Provan (1980), board size is one of the strongest predictors of organizational effectiveness in the human service sector. Chaganti et. al. (1985) compared the board size of failed and non-failed firms in the retailing industry and found that larger boards were associated with a higher rate of corporate survival. Pearce and Zahra (1992) found a significant positive relationship between board size and different measures of financial performance, using data from Fortune 500 industrial companies. In contrast, more recent studies reported

opposite results. Yermack (1996) found a negative relationship between board size and firm market value, using a sample of large US public companies. Similar results were reported using European data. Eisenberg et. al. (1998) studied small non-listed Finnish firms and found a negative correlation between a firm's profitability and the size of its board, while the study of Conyon and Peck (1998) shows an inverse relationship between return on shareholders' equity and board size for five European countries.

Second, from a completely different angle, boards of directors are *approached as decision-making groups*. In this respect, board size serves as a proxy measure of directors' expertise. Larger boards are likely to have more knowledge and skill at their disposal and the ability of boards to draw on a variety of perspectives likely contributes to the quality of the decision-making (Forbes and Milliken, 1999). However, expanding the number of directors might significantly inhibit the working of a board, due to the potential group dynamic problems associated with larger groups (Jensen, 1993). Consequently, larger boards may be hampered in reaching a consensus on important decisions (Forbes and Milliken, 1999). A limited number of studies has empirically examined the influence of board size with respect to strategic decision-making. Judge and Zeithalm (1992) found that board size was negatively associated with board involvement in strategic decisions, concluding that when boards get too large, effective debate and discussion are limited and the interaction between individual members is lower. Goodstein et.al. (1994) have explored the effects of board size on strategic changes initiated by organizations. Their results indicate that large boards have limited effectiveness in directing strategic change during periods of environmental turbulence. Also, Golden and Zajac (2001) found that strategic change is significantly affected by board size. In particular, their findings indicate that an increase in board size is negatively related to strategic change for larger boards.

To summarize, the above mentioned studies show that there is no robust evidence on the relationship between structural characteristics of boards of directors and board or company performance. Although these studies revealed interesting and useful insights, the absence of clear empirical support of substantive relationships casts doubt on both the

efficacy of agency theory as the dominant governance theory and the appropriateness of structural board measures as adequate proxies for understanding board effectiveness. In particular, the vast majority of empirical studies are being criticized for using a too narrow focus in assessing the effectiveness of boards in performing their governance role and its contribution to firm financial performance (Daily et al., 2003). It seems that our knowledge on the effectiveness of boards is hampered not only by the applied data gathering techniques, but also by inadequate attention to the potentially large number of intervening variables between board characteristics and performance outcomes (Roberts et al., 2005; Pettigrew, 1992).

4.3 Methods

As indicated in Chapter 3, the vast majority of studies on boards of directors have relied upon quantitative data gathering techniques (Daily et.al., 2003). These techniques include mainly large scale archival data, while a subset of board studies has also used questionnaires. Although these techniques offer the advantage to analyse the data in a consistent way, their access to process-oriented data is restricted (Daily et.al., 2003). Some scholars have overcome this limitation by using in-depth interviews (Roberts et al., 2005; Pettigrew and McNulty, 1998; Demb and Neubauer, 1992; Lorsch and MacIver, 1989) and direct observation techniques (Huse and Schoning, 2004; Leblanc and Gillies, 2003). Their research provides an important qualitative counter-balance to the traditional surveys on boards of directors.

In our study, we build upon the strengths of both approaches by opting for a mixed methods research design (Teddlie and Tashakkori, 2003). More specifically, we opted for a sequential exploratory design (Creswell et. al., 2003). A specific feature of this design is its two-phase approach whereby the collection and analysis of the qualitative data in an initial phase is followed by a phase of quantitative data collection and analysis. More specifically, in the first (qualitative) research phase we try to identify - by means of interviews - the full set of criteria that potentially contributes to the effectiveness of

boards. The results are then used to construct a rating survey for the second (quantitative) research phase which helps us to elaborate and interpret the qualitative findings. Furthermore, the research design implies completely different samples and data collection techniques for the two phases. We refer to Chapter 3 for a more detailed explanation of this research design.

4.3.1 Sample and data collection for the qualitative phase

4.3.1.1 Sample

For the first qualitative research phase, we selected purposefully utilizing a critical cases sampling scheme (Collins et.al., 2006) (see Chapter 3 for a detailed explanation). This means we intentionally limited the sample to members of the boards of directors of Belgian listed companies because we believed that they are well-placed to provide us with compelling insights into the determinants of board effectiveness. A sample of 147 directors of Belgian companies listed on Euronext Brussels was contacted and asked to participate in a large scale in-depth study on corporate governance in Belgium. Our sample included different directors' roles such as chairmen, non-executive directors (including independent directors) and executive directors (including CEOs). Information on the companies listed on Euronext Brussels was found on the Euronext website (www.euronext.com). Information on the boards of directors was retrieved from multiple sources such as the company's annual report, its website and the Belfirst database. Of the initial 147 directors that were contacted, a total of 104 (response rate = 71 %) agreed to participate. Table 12 presents our sample in terms of directors' roles.

Table 12: (qualitative) sample per directors' role

<i>Directors' role</i>	<i>Number</i>
Chairmen	41
Chairman = CEO	18
Chairman = independent director	11
Chairman = non-executive director	12
Executive directors	35
CEOs	30
Other executives	5
Non-executive directors	25
Independent directors	21
Non-executive shareholders' representatives	4
Secretary-generals	3
Total	104

4.3.1.2 Data collection

Data was collected during interviews with directors of Belgian listed companies. For the purpose of this study, a standardized open-ended question was used (Johnson and Turner, 2003) (see Chapter 3 for a more detailed explanation). In particular, the directors were asked to sum up what they perceived as the most important ingredients of a good board of directors. In this respect, multiple answers could be given. We deliberately opted not to use the term 'effective' to avoid misunderstanding because the concept of effectiveness may yield different interpretations. By consequence, we used the word 'good'. By phrasing the question in a more neutral way, we believed that each respondent had the same understanding of the question, which diminishes bias in the answers. In addition, by using an open-ended question we were able to fully capture a broad spectrum of criteria.

4.3.2 Sample and data collection for the quantitative phase

4.3.2.1 Sample

For the second quantitative research phase, we selected purposefully utilizing a convenience sampling scheme (Collins et.al., 2006) (see Chapter 3 for a detailed explanation). This means that we have chosen individuals that are conveniently available and willing to participate in the study. A sample of 715 members of the Belgian Governance Institute were contacted and asked to participate in our study. Members include (i) directors with different roles (such as chairmen, independent-, non-executive- or executive directors) representing boards of directors of listed as well as non-listed companies, and (ii) actors in the field of corporate governance (advisors, lawyers, academics etc.). Of the initial 715 directors that were contacted, a total of 166 (response rate = 23%) respondents were engaged in the quantitative research phase. Next, in order to avoid overlap between the samples, we excluded the respondents who previously participated in the interviews. Incomplete responses were also rejected from the sample resulting in a total of 150 (response rate = 21%). The sample can be divided in two groups of respondents. We labelled a group “directors”, representing those persons who sit on boards of directors of Belgian companies and another group received the label “experts”, representing actors in the field of corporate governance (see Table 13).

Table 13: (quantitative) sample per group of respondents

<i>Respondent</i>	<i>Number</i>
Directors	119
Representing listed companies	12
Representing non-listed companies	107
Experts	31
Total	150

4.3.2.2 Data collection

Two small written questionnaires were used to collect the quantitative data (see Appendix 3). The aim of the questionnaires was to reveal further gradation between various criteria which are assumed to contribute to the effectiveness of boards. For that purpose, we opted for structured closed-ended questionnaires whereby the response category took the form of rankings (see Chapter 3 for a detailed explanation). The 10 questionnaire items were based on the themes (representing groupings of similar criteria) derived from the open-ended question in the qualitative phase. To avoid misunderstanding, we clearly defined what was meant by board effectiveness. In particular, board effectiveness was defined as “the degree to which the board is able to carry out its strategic and monitoring tasks”. Furthermore, we also indicated how the rankings should be interpreted. To minimize response bias, the respondents received the questionnaires in two steps. As previously explained, the first questionnaire was submitted to the respondents who were asked to rank the items according to their importance (1 most important - 10 least important). After a period of time, the respondents received the second form and were asked to indicate to what extent there is room for improvement in practice (1 needs most improvement - 10 needs least improvement).

4.4 Results

4.4.1 *Qualitative analysis*

The interviews yielded a broad set of responses regarding criteria that constitute a good corporate board, as perceived by the directors. The qualitative data was analysed by coding using the ATLAS.ti software (see also Chapter 3). As recommended in literature (Miles and Huberman, 1984), we developed a coding list, based upon the literature on boards of directors and insights into the corporate governance codes, and complemented the list with topics that emerged during data analysis. This resulted in a total of 31

qualitative codes. The codes resemble as close as possible the directors' responses. In the next step, we grouped codes that related to similar themes and entered these groupings as "families" in ATLAS.ti. (see Appendix 1). The creation of families is a way to form clusters and allow easier handling of coded material (ATLAS.ti, 2004). In addition, we used a basic form of counting during the analysis process because it allowed us to more fully describe the variety of criteria that were cited during the interviews and it helped to maintain analytical integrity (Onwuegbuzie and Teddlie, 2003). Table 14 provides a summary of the results. A detailed overview of the frequencies of each individual code within a "family" can be found in Appendix 4.

Table 14: ingredients of a good corporate board - directors' perspectives

<i>Families</i>	<i>Number of respondents who referred to this theme</i>	<i>% of respondents (N=104)</i>	<i>Frequency this theme was reported</i>
Theme 1: board composition	99	95%	N=101
Theme 2: board culture	53	51%	N=55
Theme 3: operation of the board	49	47%	N=54
Theme 4: board tasks	34	33%	N=37
Theme 5: debate/decision-making	28	27%	N=29
Theme 6: individual norms	25	24%	N=28
Theme 7: relationships between the board members	23	22%	N=23
Theme 8: board-management relationship	6	6%	N=7

The findings presented in Table 14 show that aspects related to the composition of the board are - by far - most frequently reported by a large number of directors. Board culture, which expresses more intangible aspects of the board of directors, resides in the second place, closely followed by the operation of the board. The least frequently mentioned theme refers to the relationship of the board with management. In what follows, each of the themes will be described in more detail.

- **Board composition**⁷

In directors' perceptions, in order to be effective, the board of directors should have the appropriate structure. This involves several related dimensions. The most frequently cited dimension refers to *diversity*. The board should comprise a mix of people having different personalities, educational, occupational and functional backgrounds. As some directors pointed out: "A board of directors composed of 'clones' does not work". However, although diversity seems to be top of mind, it is closely followed by the dimension of *complementarity*. Having different skills at the disposal of boards is a minimum requirement, but they should be complementary. One director summarized this, using the following metaphor: "It is the mayonnaise that counts within a board, thanks to the different oils present". The third dimension relates to the *competence* of individual directors. Beyond diversity and complementarity, this dimension was cited separately as one of the key criteria. It was pointed out that individual directors should have a minimum degree of knowledge and experience. It boils down to the capacity and quality of the people sitting on the board. Within the cluster relating to board composition, the *proportion of independent directors* as well as *the size of the board* were amongst the least frequently reported criteria. In the cases where these criteria came across, it was noted that the board of directors should pursue a balance between executive directors, shareholders' representatives and independent directors. Moreover, the board of directors should not be too large.

- **Board culture**⁸

Directors also directed much attention to the more intangible side of board conduct. We labelled this theme 'board culture' - referring to a set of informal unwritten rules which regulates board and directors' behaviour. The frequencies of the reported issues, within this theme, are very close. Most important there should be *openness* and transparency. Directors should have the ability to express their views and a culture of open debate should reign. This implies that matters should be treated inside the boardroom and not

⁷ See Appendix 4, Table A

⁸ See Appendix 4, Table B

'behind the scene'. One director formulated it as follows : "There should be no taboo. All subjects ought to be touched upon. Directors should utter their opposition against a principle. Freedom of thought is very important." Second, *involvement* is also perceived as an important criterion. In contrast to a ceremonial, passive board, a good board of directors is active, interested and of added value to a company. Third, the general *atmosphere or climate* determines to some extent the way board members are expected to behave. This refers to a sense of humour, positive and constructive attitude, degree of professionalism etc.. Other dimensions with respect to board culture, less often reported, are the facts that the board members need to pursue *a common vision* or interest and be vigilant and *critical*.

- **Operation of the board⁹**

It seems that directors attach much importance to the operation of the board of directors. In particular, the *preparation* of a board meeting was often cited as a key issue. This relates to the make-up of a board agenda and, even more vital, to the documents the directors receive in advance. A director commented: "A good board must be conscientiously prepared; sufficient information must be provided for each point on the agenda in such a manner that it allows directors to decide with full knowledge during board meetings". Next, the *role of the chairman* was acknowledged. One director put it as follows: "The chairman is the driving force.... he is responsible for an efficient course of board meeting, he is the one who takes the plunge in case of conflict, who dares to stick his neck out... in addition, he is the hinge between shareholders, management and the board." Finally some aspects which were less frequently reported, related to the *conduct of board meetings* such as the length of board meetings (not too long), the quality of (management) presentations, time management etc.

⁹ See Appendix 4, Table C

- **Board tasks**¹⁰

From a different perspective, a good board of directors was viewed in relation to the tasks it performs. Particularly, directors place emphasis on *the strategic role* of the board. As pointed out by the directors, the board should be involved in determining the long term strategic direction of the company. In doing so, two additional comments are of interest. First, the board must have some insight into the evolution of the business environment. One director explained “A good board of directors is able to see the present, whilst keeping an eye on the future”. Second, the board must be able to translate the shareholder’s strategic ambitions to management. One director expressed this as follows: “See the company through the eyes of the shareholder”. In second order, the *support role* was mentioned. This role refers to the support the board of directors provides to management by means of challenging, advising and stimulating management. Some directors summarized this as follows: “A good board brings out the best in its management”. Less attention is paid to the *monitoring role* of the board and the *context* which enables a board to fulfil its tasks. The latter refers to the degree of delegation of power within the corporate governance tripod.

- **Debate/decision-making**¹¹

This theme approaches the board of directors as a decision-making group. In particular, the *occurrence and quality of the debate(s)* are perceived as key criteria. The board is not a rubber-stamping body. Real, in-depth discussion should take place but the deliberations should be characterised by neutrality and objectivity. Or as one director stated: “One should play the ball, not the man”. To a less extent, references were also made to the facts that directors should make a *contribution* in the discussions by sharing information or knowledge, and that the board should come to a *decision*.

¹⁰ See Appendix 4, Table D

¹¹ See Appendix 4, Table E

- **Individual norms**¹²

We have already touched upon the capacity and quality of the individual directors when discussing the composition of the board. In addition, more behavioural characteristics were highlighted during the interviews which we labelled as ‘individual norms’. First, the *personality* of individual directors seems to matter. In particular, aspects such as integrity, ethics, attitude, ego etc. were mentioned. Second, it also includes the *commitment* of individual directors - referring to the personal enthusiasm, interest and availability of people sitting on a board. The *independence* of and *preparation* by individual directors were perceived as less important characteristics.

- **Relationship between the board members**¹³

Directors also paid some attention to the interpersonal relationships between board members. Although the frequencies are quite low, some related dimensions could be singled out. First, boards need the right chemistry to foster *cohesiveness*. Second, *informal contacts* and interaction between the directors must be stimulated. Third, the board of directors should function as a *team*. Finally, *trust and respect* between the members are also valued.

- **Board-management relationship**¹⁴

The last theme refers to dimensions regarding the *relationship between the board and management*, which could not be grouped within the support role of the board. More specifically, this theme relates to the contact, symbioses with and trust in management, as well as to the quality of management. In fact, only a few directors mentioned the reliance on a strong and honest management as a key criterion for a good board of directors.

¹² See Appendix 4, Table F

¹³ See Appendix 4, Table G

¹⁴ See Appendix 4, Table H

4.4.2 Quantitative analysis

The previous section has provided a descriptive analysis of the variety of criteria that potentially contribute to the effectiveness of boards. By means of two written questionnaires, the qualitative findings are further elaborated. More specifically, the questionnaires offered respondents a set of 10 determinants of board effectiveness. These determinants are retrieved from the qualitative results, and as such, are not mutually exclusive, as some are closely related. The first questionnaire was aimed at getting a more profound insight into the importance rate of a select number of suggested determinants on a more quantitative base. Descriptive statistics for the full sample are given in Table 15 while Appendix 5 provides the detailed frequency table.

Table 15: descriptive statistics of importance rate for the full sample (N=150)

<i>Determinants of board effectiveness</i>	<i>in top 3*</i>		<i>Rank</i>
	<i>#</i>	<i>%</i>	
Trust between the board of directors and CEO/management	76	50,6	1
Complementarity with respect to background, expertise and experience	68	45,3	2
Board members show a constructive critical attitude	68	45,3	2
The board of directors includes a mix of executives, independent directors and non-executives representing the shareholders	61	40,6	4
The board members are well-prepared	60	40,0	5
The information is sufficient and on time	49	32,6	6
All directors actively participate in the discussions	29	19,3	7
Divergent opinions are tolerated	22	14,6	8
The chairman seeks consensus	11	7,3	9
Board members get along very well	6	4,0	10

* denotes the frequency the item received a ranking score ≤ 3

The results show that a relationship of trust between the board and CEO/management is perceived to be the most important determinant of board effectiveness. The next-best determinants are the composition of the board in terms of complementary expertise, and a constructive critical attitude of board members. In contrast, a chairman who seeks

consensus as well as board members who get along very well appear to be of little importance for the effectiveness of boards.

In order to reveal a more fine-grained view on the importance rate, we have divided our sample into two groups. A first group represents the “directors” while a second group represents the “experts”. In fact, we are interested to see if directors’ perceptions on the determinants of board effectiveness differ from those of experts in the field of corporate governance. Table 16 presents the descriptive statistics for both groups.

Table 16: descriptive statistics of importance rate for sub-samples

<i>Determinants of board effectiveness</i>	<i>DIRECTORS (N=119)</i>			<i>EXPERTS (N=31)</i>		
	<i>in top 3*</i>			<i>in top 3*</i>		
	<i>#</i>	<i>%</i>	<i>Rank</i>	<i>#</i>	<i>%</i>	<i>Rank</i>
Trust between the board of directors and CEO/management	59	49,6	1	17	54,8	1
Board members show a constructive critical attitude	58	48,7	2	13	32,3	5
Complementarity with respect to background, expertise and experience	51	42,9	3	17	54,8	1
The board of directors includes a mix of executives, independent directors and non-executives representing the shareholders	47	39,5	4	14	45,2	3
The board members are well-prepared	46	38,7	5	14	45,2	3
The information is sufficient and on time	37	31,1	6	12	38,7	6
All directors actively participate in the discussions	27	22,7	7	2	6,5	8
Divergent opinions are tolerated	17	14,3	8	5	16,1	7
The chairman seeks consensus	10	8,4	9	1	3,2	9
Board members get along very well	5	4,2	10	1	3,2	9

* denotes the frequency the item received a ranking score ≤ 3

The descriptive results indicate some differences between the perceptions of directors and experts with respect to the importance rate, as only 3 of the 10 suggested determinants rank the same (trust between the board and CEO/management, sufficient and timely information, consensus-seeking by the chairman). The views of directors and experts

diverge, in particular, regarding the importance of board members' constructive critical attitude. The deviation in the ranking score is the greatest for this determinant (ranked 2nd for directors while 5th for experts). Although our data set can be claimed for statistical ordinal testing, it does not fulfil the requirements for the computation of a Pearson Chi-Square correlation coefficient mainly because of low frequencies per cell (with respect to the responses of the expert group).

The second questionnaire was used to explore how the suggested determinants occur in practice. In particular, it yielded quantitative data reflecting respondents' perceptions on the (same) listed items in terms of their need for improvement. Descriptives of the corrigible rate for the full sample are given in Table 17 while Appendix 5 provides the detailed frequency table.

Table 17: descriptive statistics of corrigible rate for the full sample (N=75)

<i>Determinants of board effectiveness</i>	<i>in top 3*</i>		<i>rank</i>
	<i>#</i>	<i>%</i>	
The board members are well-prepared	48	64,0	1
The information is sufficient and on time	43	57,3	2
All directors actively participate in the discussions	32	42,7	3
Complementarity with respect to background, expertise and experience	31	41,3	4
Board members show a constructive critical attitude	21	28,0	5
The board of directors includes a mix of executives, independent directors and non-executives representing the shareholders	21	28,0	6
Divergent opinions are tolerated	11	14,7	7
Trust between the board of directors and CEO/management	8	10,7	8
The chairman seeks consensus	6	8,0	9
Board members get along very well	4	5,3	10

* denotes the frequency the item received a ranking score ≤ 3

The results indicate that the preparation of board members, a sufficient and timely information flow and the active participation in discussions by all directors are most in need of improvement. In contrast, consensus-driven deliberations, guided by the

chairman and a good relationship amongst the board members are perceived to be least in need of improvement.

Similar to the analysis of the importance scores, it is possible to reveal a more fine-grained view on the corrigible rate, by dividing our sample into two groups. A first group represents the “directors”, while a second group represents the “experts”. In fact, we are interested to see if directors and experts view the need for improvement of the suggested determinants differently. Table 18 presents the descriptive statistics for both groups.

Table 18: descriptive statistics of corrigible rate for sub-samples

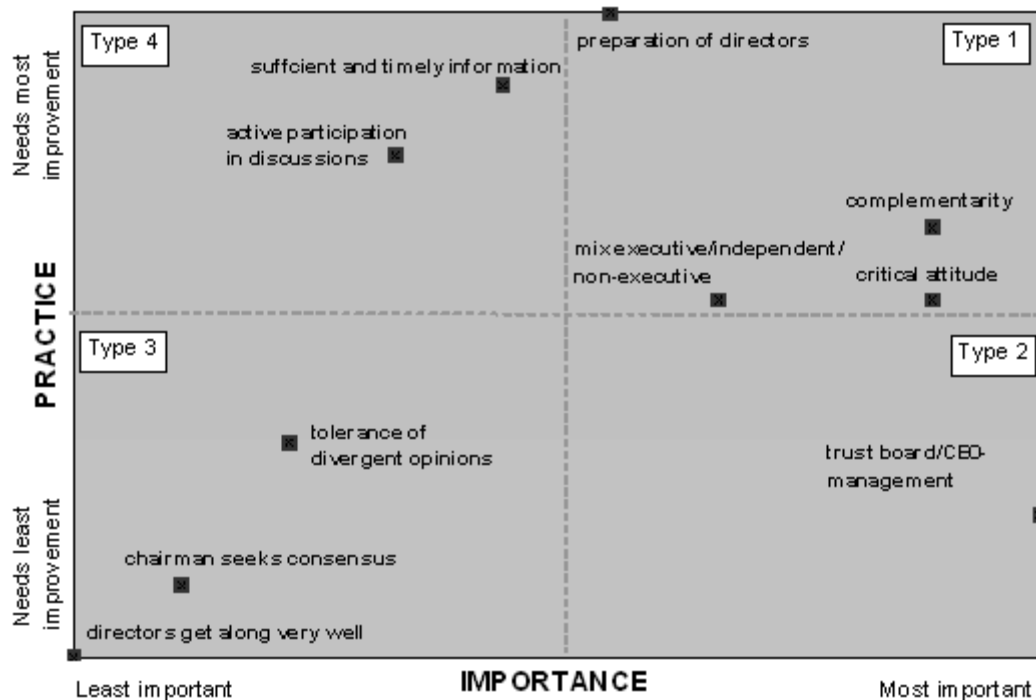
	<i>DIRECTORS (N=56)</i>			<i>EXPERTS (N=19)</i>		
	<i>in top 3*</i>			<i>in top 3*</i>		
<i>Determinants of board effectiveness</i>	<i>#</i>	<i>%</i>	<i>rank</i>	<i>#</i>	<i>%</i>	<i>rank</i>
The board members are well-prepared	37	66,1	1	11	57,9	1
The information is sufficient and on time	33	58,9	2	10	52,6	2
All directors actively participate in the discussions	25	44,6	3	7	36,8	3
Complementarity with respect to background, expertise and experience	25	44,6	4	6	31,6	4
Board members show a constructive critical attitude	16	28,6	5	5	26,3	5
The board of directors includes a mix of executives, independent directors and non-executives representing the shareholders	16	28,6	5	5	26,3	5
Divergent opinions are tolerated	6	10,7	7	5	26,3	5
Trust between the board of directors and CEO/management	6	10,7	8	2	10,5	9
The chairman seeks consensus	2	3,6	9	4	21,1	8
Board members get along very well	2	3,6	9	2	10,5	9

The descriptive results indicate great similarities between the perceptions of directors and experts with respect to the corrigible rate, as 7 of the 10 suggested determinants rank the same. The views of directors and experts seem only to diverge regarding the need for improvement of tolerating divergent opinions, trust between the board of directors and CEO/management and consensus-seeking by the chairman. Although our data set can be

claimed for statistical ordinal testing, it does not fulfil the requirements for the computation of a Pearson Chi-Square correlation coefficient mainly because of low frequencies per cell.

Finally, matching the importance rate of the determinants of board effectiveness to their corrigible rate reveals the gaps that exist, and at the same time points out the criteria that limit the board’s potential to fulfil its strategic and monitoring role. Figure 11: linking importance and corrigible scores of determinants of board effectiveness illustrates the link between the importance of the 10 suggested determinants of board effectiveness and their need for improvement.

Figure 11: linking importance and corrigible scores of determinants of board effectiveness



Quadrant 1 denotes determinants of board effectiveness representing ‘type 1’ which we term *flashing lights*. In particular, this quadrant groups criteria which are perceived to be very important for the effectiveness of boards and at the same time require most improvement in practice. Put differently, the findings suggest that too little complementarity in the expertise present, the absence of a critical attitude in discussions,

insufficient diversity regarding directors' roles or unprepared board members may hamper the board in carrying out its duties.

Quadrant 2 denotes determinants of board effectiveness representing 'type 2' which we term *challengers*. In particular, this quadrant groups criteria which are perceived to be very important for the effectiveness of boards while at the same time require only little or no improvement in practice. It appears that only one criterion fits into this quadrant, that is the relationship between the board and management. Although this relationship seems not to pose many problems in practice, the challenge to maintain a balance of trust between the board of directors and CEO/management is inherent in the governance of every company. A relationship of trust can easily be broken at any point in time and therefore requires continuous effort of both governing bodies.

Quadrant 3 denotes determinants of board effectiveness representing 'type 3' which we term *subordinates*. In particular, this quadrant groups criteria which are perceived to be of less importance for the effectiveness of boards and at the same time require only little or no improvement in practice. These criteria are perceived to be inferior compared to the other groups. Our findings suggest that a tolerance of divergent opinions in board meetings, a chairman who seeks consensus or directors who are getting along do not significantly add value to the ability of a board in performing its roles (compared to type 1 and type 2).

Quadrant 4 denotes determinants of board effectiveness representing 'type 4' which we term *seducers*. In particular, this quadrant groups criteria which are perceived to be of less importance for the effectiveness of boards while at the same time being most corrigible in practice. The findings suggest that appropriate information beforehand and an active participation of all directors in discussions are two criteria which should be addressed as practice shows major shortcomings on these issues. Still, the danger exists that these criteria might mislead attention and effort from the more critical aspects of board effectiveness (type 1 and type 2).

4.5 Discussion

Three major points emerge from this study. First, there appears to be *a gap between a limited number of structural board measures consistently found in literature and the broad set of criteria that are emphasized in directors' perceptions, in particular the systematic occurrence of a set of behavioural criteria of board effectiveness*. Mainstream board research has been heavily influenced by a research tradition from financial economics and theories treating the board of directors as a “black box”. Although boards of directors are frequently studied in academic research, scholars have traditionally focused on a limited number of characteristics such as board size, board composition and board leadership. These structural measures are commonly viewed as appropriate and adequate proxies for understanding board effectiveness, while the working processes of boards or individual directors' behaviour are rarely investigated. As such, the various research streams suggest that if the structure of a board is appropriate, the board should be able to fulfil its duties, and ultimately enhance corporate performance. However, little convincing evidence exists that these structural measures, which are presumed to contribute to the effectiveness of boards as guardians of shareholders' welfare, have had considerable impact on the financial performance of companies. Moreover, the data collected in this study reveals a huge discrepancy between the criteria found in academic literature and the perceptions of the directors themselves. Our qualitative findings have revealed an enlarged set of board attributes and suggest a more prominent role for intangible or ‘soft’ factors as determinants of board effectiveness. More than half of the directors interviewed put great emphasis on the informal rules which regulate board and directors' behaviour (‘board culture’), while more than a fourth stressed the importance of debate as a criteria for a good corporate board. The quantitative results retrieved from the questionnaires elaborate on this qualitative evidence. They highlight the importance of trust between the board and CEO/management as well as the behaviour of board members with respect to their preparation, participation and critical attitude in boardroom deliberations. Our findings suggest that boards of directors and board effectiveness in particular, should also be understood through attributes reflecting the board's inner workings and not solely through attributes of board structure and composition.

Furthermore, our findings are to a large extent consistent and supported with evidence from other qualitative board studies. The latter has also drawn attention to the importance of the human element in board effectiveness. A climate of trust and candour, a culture of open dissent, collective wisdom, collective strength and behavioural expectations are some of the elements put forward to increase board performance (Leblanc and Gillies, 2005; Charan, 2005; Carter and Lorsch, 2004; Sonnenfeld, 2002).

A second major point is that *the value of independence may be overemphasized at the cost of the broader issue of diversity*. Stimulated by the dominance of the agency perspective in corporate governance, board effectiveness has commonly been approached as the ability of boards to act independently from management. Board independence has been the cornerstone of the corporate governance debate, although considerable divergent views exist both on the right proportion of independent directors and their definition (Van den Berghe and Baelden, 2005; Daily et.al. 1999). It is assumed that independent directors add real value to a company and arguments in favour of their appointment are well-documented (Felton et.al., 1995). Corporate governance reforms tend to support the plea for board independence by advocating that a critical mass of independent directors is essential for a board to be able to provide critical oversight. Although our findings also highlight the importance of having a sufficient mix of directors' roles in terms of executives, non-executives and independent directors, they suggest that competencies, diversity and complementarity are more pivotal attributes for board effectiveness. These criteria were amongst the most cited in the interviews and the dimension of complementarity systematically received high rankings in the questionnaires. Still, the issue of diversity is to a large extent neglected in board research in spite of the fact that a small number of studies already presented interesting findings. For example, Golden and Zajac (2001) found that specific types of directors' expertise or experience are influential in shaping the orientation of a board toward strategic change. In addition, corporate governance and shareholder activists are increasingly becoming convinced by the added value of diversity in terms of improved decision-making. Boards have commonly been viewed as homogenous groups of executive and non-executive directors who are cut from the same cloth and it is argued that this uniformity undermines the quality and variety of

boardroom debate (Grady, 1999). Consequently, institutional investors have begun to pressure companies to diversify their board composition with respect to gender, race and type of expertise. TIAA-CREF, for example, puts major focus on qualified directors who reflect a diversity of background and experience (TIAA-CREF, 2006).

A third major issue is that mainstream board research ignores to a large extent *two additional conditions* under which a board of directors can make an effective contribution to the strategic direction and control of a company. First, our findings suggest that *board members should become sufficiently knowledgeable about the particular company context*. During the interviews, the aspect of preparation of board meetings in terms of agenda and information provided to directors was frequently cited. The quantitative evidence endorsed this finding as both timely and sufficient information and the preparation of board members received relatively high ranking scores as important determinants of board effectiveness. Besides, this issue was listed on top in the corrigible ranking. The need to adequately inform board members is also recognized by other scholars involved in qualitative board research. It is generally accepted that non-executive and independent directors face a disadvantageous position with regard to information gathering. Non-executive and independent directors, who spend only a limited amount of time with the company, can never know as much as the executive directors. They depend to a large extent on the goodwill of management to obtain relevant and timely information. Consequently, it is assumed that in order to be able to perform their duties, directors need to be well informed at all times (Charan, 1998). The corporate scandals are only some examples of boards that knew too little too late. In addition, it is noted that a dysfunctional information flow may hinder the performance of boards. Some boards receive bundles of documents, but only a small part may be useful in gaining an understanding of the real issues the board should be addressing (Monk and Minow, 1996). Also Lorsch and MacIver (1989), in studying American boards, reported that information is often provided in such a complex way that directors have a problem in interpreting and using it. A study by Lawler et. al. (2001) points out that those boards whose directors have a greater amount of relevant information appear to perform their roles more effectively than boards that are less well-informed.

Second, our findings suggest a pivotal *role of the chairman* in the effectiveness of boards. In particular, the qualitative data suggests that the leadership style of the chairman plays a important role in the way the board is able to carry out its duties. However, the academic governance literature traditionally looks at the issue of board leadership in quite narrow terms by focusing the discussion on the relationship of the chairman and the CEO. Especially, the question whether the two functions should be separated or not has received considerable attention and continues to be subject to much debate. Still, the effects of a separation of roles have not been consistently substantiated by empirical evidence. Besides, only a handful of studies exist which have examined the role of the chairman and his impact on the effectiveness of boards. For example, Roberts (2002) documents how the unskilful management of board relationships and processes can easily disable a board in its decision-making and performance. Based on the nature of chairman/chief executive relationships, he distinguishes three dysfunctional board dynamics – a competitive, personal and captured board - with negative consequences for board effectiveness. Also the earlier study of Pettigrew and McNulty (1995) already pointed to the key role a chairman plays in shaping board dynamics and transforming a ‘minimalist’ board to a ‘maximalist’ board, having a strong impact on the direction of a company. However, an unexpected finding in our study relates to the role of the chairman in the board’s decision-making process. The results from the written questionnaire suggest that in order for the board to be effective, it is not important that a chairman seeks consensus. As such, this finding does not support the study of Hill (1995) who found that maintaining boardroom consensus was a fundamental value amongst all directors he surveyed and that it was definitely the norm within the executive grouping. A possible explanation relates to the interpretation of the notion of consensus. Additional comments by directors revealed that consensus might be (wrongly) interpreted as ‘unanimity’ and consequently bias responses. They noted that a good board of directors reaches a decision that is supported by all board members even though personal disagreement exists.

4.6 Conclusion

The purpose of this study was to obtain a better understanding of the various criteria that (potentially) contribute to the effectiveness of boards. In order to do so, we conducted an in-depth review of the literature and complemented the insights with the findings of an extensive field study. The analysis is primarily intended to be exploratory and descriptive while using both qualitative and quantitative data. The first research phase is based on a large number of interviews and yielded a broad spectrum of criteria that constitutes a good board of directors, as perceived by the directors. By coding the criteria and clustering them into separate groups we were able to grasp the variety of criteria. Moreover, the technique of counting (the frequency a criterion was mentioned) provided a first indication of which criteria mattered more. The importance rate of a limited number of suggested determinants of board effectiveness was further examined in the quantitative research phase by means of a written questionnaire. In addition, a second questionnaire was used to further elaborate the findings by exploring how the suggested determinants occur in practice. The overall results raised three major issues which were then discussed more in-depth. What becomes clear through our research is that many aspects of board effectiveness are invisible to 'outsiders' and as a result poorly understood. Most researchers have remained at a considerable distance from actual board practice, partly because of difficulties of gaining access. As a consequence, their attention has focused on a small number of structural board characteristics leading to inconclusive findings. Our findings suggest that this ambiguity in current research evidence can to some extent be attributed to the ignorance of a wide range of interconnected structural (such as diversity and competence) and more behavioural factors (such as trust, attitude, norms and conduct) which actually shape the effectiveness of boards in performing their roles.

4.7 References

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5 Developing a process-oriented model for board effectiveness

5.1 Introduction

In the previous chapters, it was documented that the governance of companies and especially the board of directors is subject to considerable debate. Corporate governance has recently been put high on the agenda of policy makers and investors, mainly because of major corporate failures which alarmed the public at large. Besides, academic research has quite a long-standing history of studying boards of directors. The board of directors is a topic that has been extensively investigated in diverse disciplines such as finance, economics, management and - to a lesser extent - sociology. Particularly, in Chapter 4, we have noted that one of the most widely discussed issues concerns how to appropriately structure the board of directors and to what extent changes in the make up of the board influence company performance. In this respect, an impressive amount of empirical research has examined the consequences of different board characteristics on firm performance. What became clear is that the large majority of the academic governance literature treats structural board measures (such as board size, outsider/insider proportion and CEO duality) as appropriate and adequate proxies for understanding board effectiveness. Simultaneously, however, empirical research has failed to reveal a consistent relationship between board structure and corporate performance.

There seems to be a point of agreement in literature that progress will largely depend on a better understanding of the inner workings of a board of directors (Hermalin and Weisbach, 2000; Pettigrew, 1992). Already a small number of empirical studies offer a worthy attempt to open-up the “black box” of actual board conduct by exploring the dynamics of power and influence as well as the behaviour of board members and their relationship with management (Leblanc and Gillies, 2005; Roberts et al., 2005; Huse and Schoning, 2004; Pettigrew and McNulty, 1995). Simultaneously, some scholars have attempted to model the dynamics of boards theoretically (Huse, 2005; Nicholson and Kiel, 2004a; Sundaramurthy and Lewis, 2003; Forbes and Milliken, 1999). Our study

links up with this research stream in that it is also aimed at obtaining a more profound insight into the concept of board effectiveness by omitting a direct relationship between board characteristics and performance outcomes. Although the accents slightly differ, we share a common belief, mainly, that board effectiveness is determined by a large and interrelated set of variables which have been - to a large extent - ignored in mainstream board research. In particular, the findings of our extensive field study (see Chapter 4 for the detailed analysis of this field study) have revealed two important issues. First, the concept of diversity seems to be an additional structural board characteristic of high importance for the effectiveness of boards. Although diversity research has a long history in other settings, up to date it has been under-exposed in the context of boards. Second, we ascertain a systematic occurrence of a broad range of criteria with respect to board culture, board deliberations and directors' behaviour which can rarely be found in academic corporate governance literature.

The purpose of this chapter is to elaborate these empirical findings by examining the interrelationship amongst the different criteria while paying special attention to the more intangible aspects of board conduct as well as to the issue of diversity. Guided by existing board models, complemented with additional literature from other disciplines, significant variables will be extracted and integrated into a theoretical framework of board effectiveness. This chapter unfolds along the following lines. We begin by explaining, more in-depth, the inconclusive results found in board-performance links. Second, we briefly explain how boards of directors differ from other teams¹⁵ in an organization. Understanding the uniqueness of boards is useful because it limits the extrapolation of constructs found in other literature, in particular regarding group dynamics. Third, we develop the research framework, and based on theoretical assumptions we derive a number of propositions indicating relationships between the identified variables. We go on to discuss the limitations and the boundary conditions of the model. The chapter ends with our conclusions.

¹⁵ It must be noted that the management literature has tended to use the term "team" while academic literature has tended to use the word "group".

5.2 Explaining the inconclusive findings in board research

Many explanations can be given for the lack of consistent findings in empirical research on the relationship between the board of directors and company performance. In essence, they all boil down to two issues. These are (i) a lack of clear construct definition, and (ii) the reliance on incomplete research models.

First, *the diverging findings have been attributed to the varying definitions and operationalizations of the constructs used in empirical research.* Daily et.al. (1999), for example, identified over twenty separate ways of defining board composition. The earliest studies distinguished inside from outside directors and board composition was measured using three different approaches: (absolute) number of outsiders, industry inside-outside norm and outsider/insider proportion or dominance¹⁶ (Zahra and Pearce, 1989). Later on, researchers increasingly wanting to capture the independence of the outside directors have been separating independent directors from interdependent or affiliated directors. The latter is considered to be characterized by a lack of independence. In such an approach, board composition has been operationalized by the independent/interdependent distinction or by the proportion of affiliated directors (Dalton et.al., 1998). In addition to the complexity of uniformly defining board composition, the measurement of performance is also subject to considerable discussions (Hawawini et.al., 2003; Venkatraman and Ramanujam, 1986). Although some scholars rely on market-based measures, research on boards of directors has been dominated by accounting measures (Coles et.al., 2001; Dalton et.al., 1998). Performance measures rooted in financial accounting are being criticized because they (i) are subject to managerial manipulation, (ii) undervalue assets, (iii) are influenced by accounting standards such as depreciation policies, inventory valuation and treatment of certain revenue and expenditure items and (iv) are affected by differences in methods for consolidation of accounts (Chakravarthy, 1986). Furthermore, a review by Johnson et al. (1996) has revealed a list of distinct financial performance measures on which empirical research has

¹⁶ Proportion was calculated by dividing the number of outside or inside directors to board size. In contrast, “dominance” denoted the existence of a large majority of outside or inside directors on the boards, and was treated as a dichotomous variable (outsider versus insider-controlled)

relied, emphasizing the fact that certain measures have additionally been adjusted to account for industry effects or risk in a different manner. Consequently, the variety in definitions and measures applied in empirical research makes comparison of studies difficult and may be the cause of inconsistent findings.

Second, it can be argued that *the models used to study the relationship between the board of directors and firm performance are incomplete*. As previously pointed out in Chapter 1 and 4, the literature on boards of directors is characterized by a near universal focus on studying the direct effects of board characteristics on performance outcomes while ignoring the influence of potential intervening variables. In particular, Pettigrew (1992) observed that in mainstream board research: “great inferential leaps are made from input variables such as board composition to output variables such as board performance with no direct evidence on the processes and mechanisms which presumably link the inputs to the outputs” (p.171). More and more, researchers hold this point of view and are convinced that it is necessary to go beyond the traditional direct approach to fully understand what boards of directors actually do, how they work, and derivatively, to what extent they affect performance (Huse, 2005; Huse and Schoning 2004; Finkelstein and Mooney 2003; Daily et.al., 2003; Leblanc and Gillies 2003; Forbes and Milliken, 1999). This criticism is, however, by no means limited to board research as it is also expressed in studies on demography-performance links in other contexts. In particular, in “upper echelons” research (Hambrick and Mason, 1984), scholars came to understand that the relationships between Top Management Team (TMT) demography and organisational outcomes are mediated and/or moderated by various intervening variables, such as team processes. In their recent review, Carpenter et.al. (2004) propose and challenge organizational researchers to “carefully explore the practical and theoretical meaning of TMT demographic characteristics vis-à-vis the deeper constructs they are presumed to proxy” (p.749). This actually reinforces the call of earlier authors to omit the use of direct input-output models. Priem et.al. (1999), for example, already pointed out that upper echelon theories frequently suggest mediating variables (such as group interaction processes etc.) to explain the influence of TMT heterogeneity on firm performance, but that these mediators typically remain unmeasured. “Most research undertaken from a

demographics perspective implicitly views TMT processes as a “black box” that must be inferred because they are impractical to measure or cannot be directly observed” (p.947). The “black box” of organizational demography has also been described by Lawrence (1997) in terms of the phenomenon of ‘congruence assumption’. Based on Pfeffer’s (1983) original discussion, she noted that researchers assume demographic predictors to be congruent with subjective concepts, which therefore are irrelevant and unnecessary to include. She makes a strong case to eliminate the congruence assumption to study the actual mechanisms underlying the demography-outcome relationships. At the same time, the need for inquiry into intervening processes is strengthened by studies that have demonstrated superior explanatory power by including process variables in TMT research (Pettersen et al., 2003; Papadakis and Barwise, 2002; Amazon and Sapienza, 1997; Amazon, 1996; Smith et. al., 1994).

In this respect, TMT research and research on group effectiveness in general, offer an interesting starting point to explore the added-value of including process variables in board research. Still, it can be argued that the board of directors differs from other teams active within an organization .

5.3 Differentiating boards of directors from other organizational teams

The board of directors can be considered as a multi-member governing body, standing at the apex of the organization (Bainbridge, 2002). However, being a collection of individuals, boards of directors show some distinctive features which make them, to some extent, unique amongst organizational teams (see Table 19 for a summary).

A first feature is **partial affiliation**. Board of directors usually include outside directors who are not employees of the company and do not assume management tasks (see descriptive statistics presented in Chapter 2). In most cases, outside directors sit on several boards and these mandates come on top of their regular ‘day job’. In this respect,

outside board members are only partial affiliated to the company on whose board they serve (Forbes and Milliken, 1999; Nadler et.al., 2006). Second, boards of directors are characterised by **episodic interactions**. Most board of directors only meet a few times a year (see descriptive statistics presented in Chapter 2). Although (some) board committees meet more frequently, the meetings involve only a small subset of the whole board. By consequence, board members spend only a limited time together in the boardroom so that it is quite difficult to experience intense personal contact. Besides, with little or no contact between formal board meetings, there is little opportunity to build strong working relationships (Forbes and Milliken, 1999; Nadler et.al., 2006). A third feature is **limited time and information**. Outside board members devote only limited amount of their time to board-related work (Lorsh and MacIver, 1989). Moreover, as noted in Chapter 4, they heavily depend on the goodwill of the management to obtain relevant and timely information. In this respect, it is obvious, that outside directors - compared to executive directors - are restricted in their ability to become deeply familiar with the company, its people and its business issues (Nadler et.al., 2006). Fourth, boards of directors are commonly composed of a **preponderance of leaders**. Regarding the background of outside directors, most of them can present a track-record as former or present CEO (Forbes and Milliken, 1999). It is often because of their outstanding professional achievements that they have been appointed to the board of directors. At the same time, these individuals are used to sitting at the head of the table and have their own psychological needs for power, recognition, and influence. For many of these directors, the setting of a board of directors is (or might be) sensed as an unusual and uncomfortable situation (Nadler et.al., 2006). Fifth, **complex authority relationships** exist within a board of directors. In contrast to management teams, the role and position of outside directors do not reflect their status in the company's hierarchy (Nadler et.al., 2006). Still, some outside directors may have more authority than others, due to their status in the corporate world or business community at large. Moreover, when the positions of chairman of the board and CEO are combined, as it is still the case in many companies, a perplexing power relationship might exist (see Chapter 2 for descriptive statistics on the occurrence of CEO-duality). A sixth feature relates to the **changing expectations for work**. Compared to other teams, the role of the board is often not well-

defined and may substantially differ amongst companies. In addition, boards of directors are increasingly confronted with unprecedented scrutiny and (public) pressure (Van den Berghe and Levrau, 2004). As a result, many boards are struggling to agree on what their tasks are, also vis-à-vis management. Seventh, boards of directors expose an **aura of formality**. The format, physical setting, social rituals and conduct of a board meeting create a sense of formality and status which is uncommon amongst other teams (Nadler et.al., 2006). Finally, boards of directors encompass a **larger number of members**. On average, the number of board members exceeds the size of other organizational teams frequently studied in the literature (Forbes and Milliken, 1999) (see Chapter 2 for descriptive statistics on board size).

Table 19: characteristics differentiating boards as teams

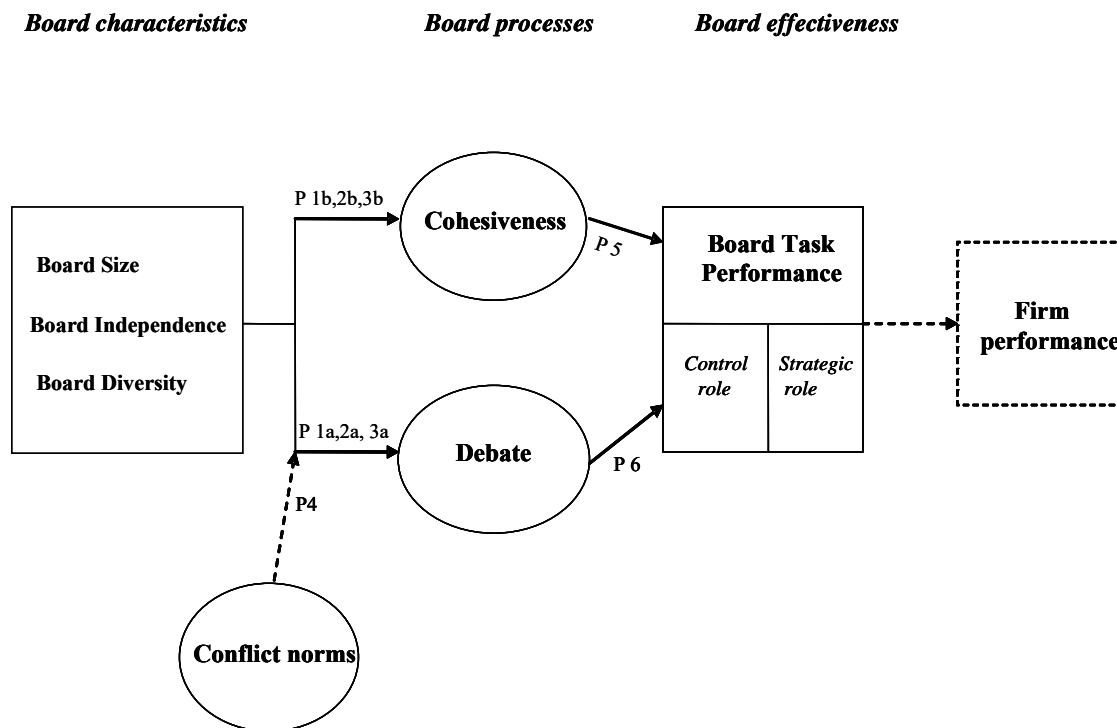
	<i>Boards as teams</i>	<i>Typical teams</i>
Affiliation	Outside directors may be members of more than one board; this is not their “day job.”	Members work for the same organization.
Interaction	Directors spend little time together, making it difficult for them to build working relationships.	Members spend considerable time together, experience intense personal interaction.
Time and information	Limited time and information available to master issues of a complex company.	Constantly immersed in company’s business.
Leaders as members	Majority of members may be CEOs, who are used to leading, not following.	Most members are not accustomed to sitting at the head of the table.
Authority relationships	Lines of authority complex and unclear; chairmen/CEOs both lead and report to boards.	Members’ roles on the team often reflect their status in the company.
Changing expectations	Difficult to achieve consensus in a climate of unprecedented scrutiny and pressure.	Usually created with a reasonably clear charter –such as completing a project- in mind.
Formality	Physical setting and social rituals reinforce aura of power and privilege.	High degree of formality is rare, generally reflects the culture of the company.
Team size	Average number of members is rather high	Average number of member is rather low

(source: adapted from Nadler et.al., 2006)

5.4 Presenting a theoretical research framework of board effectiveness

Taking into account these distinctive features, we develop a model of board effectiveness that bridges some of the gaps in the research on boards of directors (see Figure 12). Drawing on a broad variety of sources (e.g. corporate governance literature, literature on TMT and group effectiveness, field studies etc.), we distinguish multiple intervening constructs that we believe mediate the direct impact of board characteristics on firm performance. The proposed model strongly relies on the input-process-output approach used in research frameworks for studying organizational teams (e.g. Gladstein, 1984; Cohen and Baily, 1997). Apart from that, this approach also inspired existing board models (e.g. Huse, 2005; Forbes and Milliken, 1999).

Figure 12: overview of the research framework



5.4.1 Defining board effectiveness

Literature reveals that multiple approaches exist to determine the concept of effectiveness due to the scholars' different background and their heterogeneous research purposes (Van den Berghe and Levrau, 2004; Kuo 2004). In their seminal article Hackman and Morris (1975) set out three criteria of *group effectiveness*: group performance, the ability of the group to work together over time and the satisfaction of the personal needs of group members. This definition includes the classic "task" (group-produced) and "maintenance" (attitudinal) criteria and has been commonly used in research on work groups (Lemieux-Charles et. al., 2002; Cohen and Bailey 1997; Jehn 1995; Gladstein, 1984). Applied to the context of boards of directors, *board effectiveness* is mainly concerned with "task" outcomes and occurs by fulfilling a role set (Nicholson and Kiel, 2004b). The latter is, however, still subject to considerable debate in literature. The role set is often not defined as an integrated set of activities but is rather conceptualized in a multiple, and in some cases, contradictory way as a function of the underlying theory (Hung, 1998; Johnson et.al., 1996). Commonly accepted is the classification into three board roles: control, service and strategic role (Maassen,1999; Zahra and Pearce, 1989). Table 20 provides a detailed overview of a board of directors' role set.

Table 20: a board of directors' role set

	<i>Control role</i>	<i>Service role</i>	<i>Strategic role</i>
Board Responsibilities	<ul style="list-style-type: none"> • Maximizing shareholder's wealth • Primarily the board has to monitor actions of agents (executives) to ensure their efficiency and to protect principals' (owners) interests 	<ul style="list-style-type: none"> • Boards are a cooptative mechanism to extract resources vital to company performance • Boards serve a boundary spanning role • Boards enhance organizational legitimacy • Boards serve as 'sounding board' for management 	<ul style="list-style-type: none"> • Boards are rubber stamps ('passive' school of thought) • Boards are an important strategic device contributing to the overall stewardship of the company ('active' school of thought)
Board Tasks	<ul style="list-style-type: none"> • Selecting, rewarding and replacing CEO 	<ul style="list-style-type: none"> • Scanning the environment 	<ul style="list-style-type: none"> • Satisfying the requirements of

	<ul style="list-style-type: none"> Monitoring/evaluating company performance Articulating shareholders' objectives and focusing the attention of key executives on company performance Reducing agency costs Ratifying and monitoring important decisions 	<ul style="list-style-type: none"> Representing the firm in the community Securing valuable resources Providing advice to the organization and CEO Involvement in strategy formulation and implementation 	<p>company law ('passive view')</p> <p>'Active' view :</p> <ul style="list-style-type: none"> Guiding management to achieve corporate mission and objectives Involvement in the strategic decision making process
Theoretical perspectives	Legalistic Agency Theory	Resource Dependence Theory Stewardship theory	A broad range of theories e.g. managerial hegemony theory and stewardship theory
Theoretical origins	Law Economics & Finance	Organizational Theory Sociology Psychology	Organizational Theory Sociology

(Source: adapted from Zahra and Pearce. 1989)

Regarding **the control role**, the board of directors has a legal duty to provide oversight and is expected to carry out this duty with sufficient loyalty and care. Particularly, in Anglo-American countries it is emphasised that the board has a fiduciary duty to oversee the company's operations and monitor top management performance in order to protect shareholders' interests (Lorsch and MacIver, 1989). The board's duty to monitor management and corporate performance has also been addressed in other disciplines than law. In particular, the dominant theory underlying the control role of the board is agency theory, initially the prevailing school of thought in finance and economic research (Jensen and Meckling, 1976) (see also Chapter 2 for a more in-depth discussion on agency theory). In an agency perspective, the board of directors has the obligation to ensure that management acts in the interest of the shareholders. The board meets this obligation by scrutiny and evaluation of the actions of top management. In particular, a board of directors fulfils the critical tasks of hiring, firing and compensating the CEO (top management) as well as ratifying and monitoring important decisions (Fama and Jensen, 1983).

The **service role** of the board of directors primarily stems from a resource dependence view and secondly from stewardship theory (see also Chapter 2 for a more in-depth discussion on resource dependency and stewardship theory). A careful reading of the literature however reveals that the service role of the board is not uniformly approached. From a resource dependence perspective, which is mainly grounded in sociology and organizational theory, the board of directors is seen “as a vehicle for co-opting important external organizations with which the company is interdependent” (Pfeffer and Salancik, 1978). Within this context, Mintzberg (1983) distinguishes at least four service roles of the board of directors: (1) co-opting external influencers, (2) establishing contacts (and raising funds) for the organization, (3) enhancing the organization’s reputation and (4) giving advice and counsel to the organization. In particular, the latter refers to the board’s potential to provide high-level advice to the CEO (Dalton et.al., 1998; Jensen, 1993). An alternative approach of the service role, mainly based on stewardship theory, excludes legitimacy and resource dependence functions in favour of strategic engagement. This point of view suggests that the board of directors can serve the CEO and management with their expertise through their active involvement in the strategic decision-making process, particularly by advising top management on the initiation, formulation and implementation of strategy (Carpenter and Westphal, 2001; see also the review by Johnson et.al., 1996). As a consequence, this approach blurs a clear distinction between the service and the strategic role of a board of directors.

Finally, **the strategic role** of the board of directors has historically been subject to much dispute, especially in the management literature (see e.g. the discussions in various issues of Harvard Business Review from the beginning of the 1980, edited by Kenneth Andrews). The strategic role of the board taps insights from different theoretical perspectives. In essence, two broad schools of thought on the involvement of boards in strategy can be detected, referred to in the literature as “active” and “passive” (Golden and Zajac, 2001). The passive school views the board of directors as a rubber stamp or a tool of management with little or no impact on a company’s strategy process (see e.g. the discussion on the managerial hegemony perspective in Chapter 2). In contrast, the active school views the board of directors as an ‘independent’ body that actually contributes in

shaping the strategic course of a company and in guiding the management to achieve the corporate mission and objectives (Maassen, 1999; Hung, 1998). The board's contribution can occur in a myriad of ways such as through advice and counsel to the CEO, through careful refinements of strategic plans, by initiating own analyses or suggesting alternatives, by probing managerial assumptions about the firm and its environment, or by ensuring that agreement exists amongst executives on the strategic direction of the firm (Zahra, 1990; Zahra and Pearce, 1989). According to Goodstein et.al. (1990) the strategic role is of particular importance in critical cases such as periods of environmental turbulence or declines in company performance, because such events provide the opportunity to a board to initiate strategic change. As pointed out by different scholars, the active school of thought is receiving growing attention and is gaining ground (Hendry and Kiel, 2004; Finkelstein and Hambrick, 1996).

Although the literature recognizes three board roles, the importance attached to each role is not equal. As agency theory dominates corporate governance research, it is obvious that the board's control role is emphasized as the most important one and this role is well-documented by a rich body of empirical literature. At the same time, the importance of the board's strategic role is supported by a limited but increasing amount of empirical research. Several scholars have attempted to understand actual board involvement in the strategic decision-making process mainly relying on qualitative research techniques (Van den Berghe and Levrau, 2004; Short et. al., 1999; McNulty and Pettigrew, 1999; Goodstein et.al., 1994; Johnson et.al., 1993; Judge and Zeithalm, 1992; Demb and Neubauer, 1992; Lorsch and MacIver, 1989). Applied to our study, we value the view of a two-fold role set which comprises the control and the strategic role. Different arguments underpin our choice. First, previous studies on boards of directors have relied on a single theoretical perspective favouring one board role at the expense of the other, resulting in an incomplete picture (Hillman and Dalziel, 2003). In order to get a more holistic and richer understanding of what boards do, we contend that a multiple lens approach is important (see also Chapter 2). Second, as argued above, the service and strategy role are not mutually exclusive as some overlap exist with respect to the prescribed tasks performed by the board, particularly with respect to the strategic

decision-making process. Finally, the strategy role received the most attention (compared to other roles) in the directors' perceptions during our field study (see chapter 4). Therefore, we have opted to integrate the service and the strategy role. As a consequence, *in our model board task performance refers to the degree boards are successful in carrying out their strategic and monitoring tasks*. Because of the rather confidential nature of board activities, it is not easy to measure board performance in ways that are both reliable and comprehensive. A suggestion of Forbes and Milliken (1999) is to use certain publicly announced board actions, for example CEO replacement, as proxies for performance of the control functions. Still, this approach appears to be less suitable for the assessment of board task performance on the strategic dimension. In particular, it can be argued that is difficult to isolate the real impact of the board of directors (from the impact of management) when assessing publicly announced strategic decisions, such as a take-over. Alternatively, we suggest researchers to measure board task performance by identifying various board functions related to the strategic and monitoring role and then asking respondents to assess how well these functions are being performed. In spite of their limitations, these self-evaluation approaches have been commonly used in previous empirical studies on board effectiveness in the non-profit sector (e.g. Cornforth, 2001; Green and Griesinger, 1996; Bradshaw et.al., 1992; Slesinger, 1991).

So far, we have argued that the impact of boards of directors on company performance indirectly occurs through the effectiveness of boards in performing their dual key roles. In the next sections, we elaborate the indirect route by proposing three process variables that we believe will significantly influence the task performance of boards: cohesiveness, debate and conflict norms. Moreover, we capture them in a set of propositions.

5.4.2 Cohesiveness and debate as intervening variables

Despite certain distinctive characteristics, boards of directors are, like top management teams, confronted with complex ambiguous tasks. Much of the work that boards of directors must do in order to produce effective outcomes involves cooperative decision-making and joint efforts. Board members are required to work together by mutual

interaction, sharing information, resources and decisions. In this respect, the board of directors is considered to be a collegial body and only if board members coalesce into a group, can collective judgment emerge (Charan, 1998). However, it is only in the last decade that scholars began suggesting that the board should transform itself from a loose aggregation of individuals into an effective team (for example, Nadler, 2006 and 2004; Carter and Lorsch, 2004; Conger et.al., 2001). For boards of directors to become a team, that operates collegially, we argue that a minimum degree of cohesion amongst the board members is required. Our view that cohesion aids collaboration and communication amongst board members, and as such influences performance outcomes, has also been suggested and reinforced by research on other teams. Organizational demography literature has emphasised **cohesiveness** (or social integration) as a potential intervening construct and it is one of the most extensively studied variables in group settings (Williams and O'Reilly, 1998; Bettenhausen, 1991). Group cohesiveness is defined as *“the degree to which the members of the group are attracted to each other and are motivated to stay in the group”* (Shaw 1976:197). The concept is affective in nature and is characterised by a sense of connectedness. In particular, cohesiveness is considered to play a vital role in any exchange relationship (Austin, 1997) and it can be argued that it also has relevance in the context of boards of directors. To the extent board members like each other and like the group, they can be expected to interact and integrate more easily. Moreover, qualitative research by Finkelstein and Mooney (2003) as well as our own research (see Chapter 4 and Van den Berghe and Levrau, 2004) has revealed that directors value the chemistry of the board and the team spirit of their colleagues as important elements of board effectiveness. Ideas such as “team spirit” and “teamwork” have been linked to the concepts of social integration and cohesiveness (Seashore, 1977). Lastly, the board model put forward by Forbes and Milliken (1999) has also suggested that cohesiveness may exert an influence on the task performance of boards of directors. Researchers can operationalize cohesiveness by using the four-item cohesiveness index from O'Reilly et.al. (1989). In addition, directors can be asked to evaluate statements such as “members of this board respect and trust each other”, “board members also socialize with each other outside board meetings” etc.

Considering the board of directors as a decision-making group, we propose a second intervening construct, namely **debate**. Debate is defined - consistent with Simons et. al. (1999) - *as an open discussion of task-related differences and the advocacy, by different board members, of differing approaches to the decision-making tasks*. The expression of cognitive conflict during discussions is considered to be a critical component of decision-making groups: “debate is critical in liberating relevant information and shaping effective courses of action” (Eisenhardt et.al., 1997:43). Since the complexity of board’s tasks overwhelms the knowledge of one person, board members are supposed to share their own, unique experiences or perspectives via discussions or other forms of interaction (Schweiger et.al., 1989). In particular, board members must find ways to let their views be aired, to challenge one another’s viewpoint without breaking the code of congeniality. Debate facilitates the generation of ideas and provides the opportunity to critically assess multiple alternatives and to question false assumptions (Eisenhardt et.al., 1997). Debate has some overlap - but is not identical to - the concepts of task conflict, which can also be found in studies on top management teams and cognitive conflict, which is also proposed by Forbes and Millikens’ board model. Task or cognitive conflict exists when there are disagreements amongst group members about task issues, including differences in ideas and opinion on how best to perform the content of the task (Jehn, 1995). The difference with debate boils down to the fact that the concept of task conflict is essentially based on a perception of difference or disagreement which does not necessarily need to be expressed verbally (Simons et. al., 1999). Next to the recognition in literature of including debate as an intervening process variable, when studying decision-making groups, the issue has also been emphasised by the directors themselves. Our field study revealed that directors perceived the occurrence of objective debate as one of the key criteria for board effectiveness (see Chapter 4 for a detailed analysis). Our findings are consistent with the evidence of a qualitative study by Finkelstein and Mooney (2003). They noted that during their interviews, all directors mentioned the importance of constructive conflict in discussing diverse views amongst themselves and with the CEO. Debate, as a construct, can be measured by extending the scale from Simons et. al. (1999). In particular, board members can be asked to rate statements such as “discussions during the meetings are constructive”, “when discussing an issue directors state clear

disagreement with each other”, “different directors propose different approaches to the issue”, “directors openly challenge each other’s opinion” and “discussions of the issue become heated”.

5.4.3 The effects of board characteristics on board processes

Board size refers to the number of board members. It simply represents a board’s structural and compositional context. Hambrick and D’aveni (1992) state: “at a basic level, the resources available on a team result from how many people are on it” (p.1449). Board size is a well-researched characteristic as it is considered to have an important impact on the functioning of a board (see also Chapter 4). Still, the effects produced by board size are not unambiguous as they can be both positive and negative. In many studies, board size is recognized as a proxy for directors’ expertise, and in this respect, board size is synonymous with cognitive capability (Amason and Sapienza, 1997). Larger boards have the potential to provide an increased pool of expertise because their members likely have a broader variety of backgrounds and may represent more specialized knowledge and skills (Smith et.al., 1994). For this reason, larger boards are better equipped (compared to small boards) to process large amounts of information (Eisenhardt and Schoonhoven, 1990). The possibility for boards to draw on a larger pool of expertise likely contributes to the quality of the discussions in board meetings.

Jensen (1993) however contends that board size is not unlimited. There exists a turning point where the benefits of an enlarged board will be outweighed by the costs in terms of productivity losses. As size increases, boards may be confronted with some traditional group dynamic problems associated with large groups. In fact, larger boards of directors become more difficult to co-ordinate and may experience problems with communication and organization - a proposition borrowed from organizational behaviourists (see for instance Hackman, 1990; Eisenberg et.al., 1998). Consequently, boards that are too large may be inhibited to have fruitful debates. Besides, having a high number of board members around the table may hamper the board’s ability to identify, extract and use its

members' potential contribution. Given the limited time available during board meetings, there might be too many members to hear from and to persuade (Patton and Baker, 1987). Finally, larger boards - as with any large group - may find it difficult to establish the interpersonal relationships which further cohesiveness (Shaw, 1976). The problem of not developing intense personal contact in larger boards will also be strengthened by the episodic interactions amongst the board members. As a consequence, they are prone to develop factions and coalitions which can increase group conflict and hence inhibit cooperation amongst the directors (Goodstein et. al., 1994). Thus, we offer the following propositions :

Proposition 1 a : the effect of board size on debate will be positive but when the size becomes too large, the impact on debate will be negative

Proposition 1 b : the larger the size of the board, the less cohesiveness the board members will experience

Board independence refers to the degree of independent outside representation on the board of directors (Van den Berghe and De Ridder, 1999). An increase in the number of independent directors relative to executive directors is one of the commonly prescribed remedies to improve corporate governance (Walsh and Seward, 1990). The ratio of outside independent directors is frequently used as a measure of the extent to which a board is able to act independently, especially from management (see Chapter 2 and Chapter 4). Particularly, the agency perspective presumes that independent directors - irrespective of the way they are defined¹⁷ -, engage in a critical assessment of management proposals and that they take a dispassionate stand vis-à-vis management interests and values (Kosnik, 1987). Because of their non-employment status independent directors are supposed to identify with the interests of the shareholders and to operate in the best interest of the company in an unbiased and object way (Van den Berghe and

¹⁷ As indicated in Chapter 2, in countries where the Anglo-American system prevails and thus where the manager *de facto* calls the shots, independence is defined with respect to the management. In contrast, in many Continental European countries with concentrated share-ownership, independence is seen primarily in relation to the dominant shareholder.

Baelden, 2005). In other words, due to the absence of close ties with the company, independent directors are able and better placed to approach issues from a distance and to speak up more freely. In addition, the literature on director interlocks suggests that independent directors bring along important information about business practices and policies, due to their experiences on other boards. This information may further enable problem-solving and facilitates discussions (Carpenter and Westphal, 2001; Rindova, 1999). In contrast, the contribution of executives sitting on the board is believed to be less straightforward. Although executive directors may bring along firm-specific information, which is presumed to lead to a more effective decision-making process (Rosenstein and Wyatt, 1990; Fama and Jensen 1983), their willingness to be actively involved in candid discussions has been questioned. It is argued that their objectivity will be impaired by their dual role as full-time manager and executive director (Kosnik, 1987). Especially their ties and loyalty to the CEO, in addition to the fear of retaliation which could harm future working relationships or career perspectives, may prevent executive directors from openly voicing disagreement during board discussions (Baysinger and Hoskisson, 1990; Patton and Baker, 1987).

At the same time, increasing board independence, by attracting more independent directors may hamper the integration of board members. By definition, independent directors are not employees of the company and do not assume management tasks. As most boards of directors only meet a few times a year, outside independent directors interact less frequently with each other and with the executives. Moreover, they are less close-knit due to their affiliations with different firms (see section 5.3). Thus, we offer the following propositions :

Proposition 2 a : an increase in board independence will increase debate

***Proposition 2 b : an increase in board independence is negatively related
to cohesiveness***

Board diversity refers to the degree to which a board is heterogeneous with respect to informational demographic attributes (Jehn et.al., 1997). In particular, board diversity reflects differences in knowledge, experience and skills (due to educational, functional or occupational backgrounds, industry experience etc.). In the case of boards of directors, the issue of diversity is introduced by the resource dependence perspective (see also Chapter 2). By recruiting outside directors with different backgrounds or who represent specific organizations, boards of directors help to link the company to its external environment and as such secure critical resources (Pfeffer, 1972). In addition, the interest in board diversity is growing, under the pressure of major institutional investors (see for example, TIAA-CREF's policy statement dating from 1997) and other shareholder activists. Directors themselves also stressed the importance of having a diversified mix of people on the board of directors in order to be effective (see detailed analysis of our field study in Chapter 4). However, up to date the concept of diversity is a rather unexplored domain in empirical board research (Carter et. al., 2002). In contrast, research on diversity in other settings has a long-standing history. Although the issue of diversity has not been approached in a uniform way, two streams have been identified that influence the way diversity is conceptualized. One stream of research approaches diversity from a moral-ethical perspective and focuses on the social inequity in order to identify discriminatory practices in the workplace. A second research stream studies diversity from an organizational and economical perspective in order to examine the effects of diversity on work-related outcomes (Janssens and Steyaert, 2003). Especially the latter points out robust relationships which can to some extent be extrapolated to the context of boards of directors.

Diversity amongst board members is assumed to improve debate due to the obvious reason that diversity is commonly associated with different life experiences and hence diverse perspectives (Eisenhardt et.al., 1997). In fact, research on group heterogeneity suggests that creativity is positively related to skill-based heterogeneity because diverse perspectives can produce and consider a broad array of solutions and decision criteria (Schweiger et.al., 1986). This is of particular relevance when groups are confronted with complex, non-routine tasks, as it is the case with boards of directors. From a different point of view, research has also shown that board members who are in a minority position

have the potential to provide unique perspectives and challenge the conventional wisdom amongst the majority in the board (Westphal and Milton, 2000). For example, when the majority of board members represent a particular functional background (e.g. finance), the opinion expressed by a board member with a different background (e.g. marketing) may shed another light on the topic, and hence, change the discussions.

Although the results of empirical research on the cognitive capacity of groups are consistently positive (see the reviews by Milliken and Martins, 1996 and Williams and O'Reilly, 1998), if boards become too diverse, debate may be hampered by difficulties in understanding of alternatives, attributable to differences in language or background (Pelled, 1996). Board members with the same background share a language which reflects similarities in interpreting, understanding and responding to information. Directors who are not familiar with this shared language may find it difficult to communicate (Zenger and Lawrence, 1989). In addition, heterogeneous boards have a greater potential for disputes (Goodstein et.al. 1994), are less able to agree on means and objectives (Golden and Zajac, 2001) and as a consequence, may find it difficult to reach consensus.

At the same time, based on socio-psychological research, greater heterogeneity on boards is likely to have a negative impact on cohesiveness. An explanation can be found in the social categorization and similarity/attraction theory. The first refers to the process of self-categorization. The basic assumption of the social categorization theory is that individuals seek a positive self-identity. Therefore, on the base of demographic attributes, individuals classify themselves and others into social categories. This process permits the individual to define himself in terms of a social identity and to compare himself to others (Tajfel, 1982). Individuals are perceived as in-group members if they have similar features and out-group members otherwise. There is a tendency then to evaluate the members of other categories more negatively which results in stereotyping, polarization and anxiety (Tsui et. al., 1992). According to this theory, individuals tend to prefer homogeneous groups of similar persons. Diversity, in contrast will trigger the process of social categorization. The more diverse a board is composed, the greater the chance directors will be confronted with individuals of other social categories, resulting in increased hostility which may have detrimental effects on the cohesiveness within the

board. A similar prediction is grounded in the similarity/attraction paradigm. According to this perspective, individuals who perceive themselves as similar to others tend to empathize with and feel attracted to these other persons (Byrne, 1971). Similarity can appear on all kinds of attributes ranging from demographic variables to attitudes and values. Being similar reinforces a person's attitude and beliefs while dissimilarity is considered negatively (Tsui and O'Reilly, 1989). Empirical research on groups already supports these predictions. In particular, diversity on attributes like gender, race and functional background have been found to negatively influence affective outcomes such as commitment, cohesiveness (or social integration), satisfaction etc. at both the individual and group level (see Williams and O'Reilly, 1998 and Milliken and Martins, 1996 for a review). Applied to a board context, diversity, irrespective of the way it is uttered/expressed, yields dissimilarity amongst the members which lowers interpersonal attraction and liking. Thus, we advance the following propositions :

Proposition 3 a : the effect of board diversity on debate will be positive but when the board becomes too diverse, the impact on debate will be negative

Proposition 3b : the greater the diversity in the board of directors, the less cohesiveness the board members will experience

5.4.4 The moderating role of conflict norms

In addition, we expect that the strength of the relationship between board characteristics and debate, may depend on current norms regarding conflict. Norms are a set of informal, unwritten rules derived from shared beliefs which regulate board members' behaviour (Nadler, 2004;; Wageman, 1995; Shaw, 1976). Although individuals behave differently, they care about how they are perceived by other group members and strive to comport themselves in accordance with group norms (Bainbridge, 2002). Bettenhausen and Murnighan (1985) consider norms as "standards against which the person can evaluate the appropriateness of behaviour,... providing order and meaning to what otherwise

might be seen as an ambiguous, uncertain, or perhaps threatening situation” (p.350). In particular, **conflict norms** refer to standards that “*encourage an openness and acceptance of disagreement*” (Jehn, 1995). Conflict norms are suggested as a necessary condition for the emergence of debate (Faulk, 1982). Without these norms, the board of directors is unable to take advantage of its diversity and available expertise. Only if there is an atmosphere in which board members can freely express their opinions, will open discussion emerge. It is likely that directors will hesitate to be a “devil’s advocate” if board norms do not allow critical questions to be asked. Conversely, when a board of directors is characterized by a willingness to challenge and the utterance of viewpoints is expected, board members may feel encouraged to become actively involved in board discussions. This view has been reinforced by our qualitative field study. Many directors emphasized the importance of an open board culture where it is considered appropriate to engage in a vigorous debate (see Chapter 4). In addition, Amason and Sapienza (1997), found in their study on top management teams a positive impact of ‘openness’ on task conflict. Also Huse (2005) includes board culture in his research framework and has found in a recent study of Norwegian firms that ‘openness and generosity’ (one of the measures of board culture) was positively related to specific board roles. In essence, while board size, independence and diversity provide the potential for debate, conflict norms represent the catalyst that unlocks this potential. Relying on Jehn’s (1995) example, researchers could operationalize conflict norms by asking board members to rate statements such as “differences of opinions are accepted in the board”, “disagreement is detrimental to getting the work done by the board”, “critical questions are tolerated in the board”, “disagreement is dealt with openly in the board” and “directors try to avoid disagreement at all costs”. Based on the above mentioned argumentation, we offer the fourth proposition :

Proposition 4 : the greater the conflict norms, the stronger the relationships between board size, independence, diversity and debate

5.4.5 Indirect effects of board characteristics : the board processes-task performance link

The strategic as well as the control role of the board include complex and interactive tasks which require a minimum level of interpersonal attraction, or cohesiveness, amongst the board members in order to perform these tasks effectively. In particular, the performance of these tasks depends on mutual trust and professional respect and this is more difficult to sustain when boards are more fragmented (Forbes and Milliken, 1999). Genuine collegiality in the boardroom is required to foster confidence that board members are respectful listening to each others points of view and are committed to working through the board tasks in a collective way. Empirical research on other groups has already found a positive relationship between cohesiveness or social integration and performance outcomes (Cohen and Baily, 1997). Higher cohesive or integrated groups experience higher levels of member satisfaction (Bettenhausen, 1991), a higher productivity (Shaw, 1976) and a lower turnover rate (O'Reilly et.al., 1989).

Still, it can be argued that the impact of cohesiveness on board task performance is not simply linear. In fact, group studies have demonstrated that a high level of cohesiveness may lead to a pressure to conform with group standards and a striving for unanimity at the expense of critical thinking and questioning of assumptions, a phenomenon known as “groupthink” (Janis, 1983). Also boards of directors may be vulnerable to the danger of groupthink to the extent politeness and courtesy is emphasized over critical oversight and quality strategic decision-making (Jensen, 1993). In this respect, board members are failing to examine alternatives, to be critical - either to themselves or to others, and be selective in gathering information (Bainbridge, 2002). Based on these assumptions, we advance the following propositions:

Proposition 5 : the effect of cohesiveness on board task performance will be positive but when cohesiveness is too high, the impact on board task performance may be negative

As noted before, in most boards, directors are faced with complex strategic and monitoring issues. By relying on their specific expertise and backgrounds they may have different viewpoints on how to accomplish these issues and especially on what trade-offs need to be made. In view of reaching a consensus, board members are presumed to challenge and critically oppose each other's ideas. Research by Schweiger et.al (1986) suggests that the presence of debate improves group performance by formalizing and legitimizing conflict and by encouraging critical evaluation. According to Eisenhardt et.al. (1997) debate "provides a more inclusive range of information, a deeper understanding of the issues, and a richer set of possible solutions" (p.43). Simons et.al. (1999) argued that when team members are confronted with other opinions they are forced to reconsider their viewpoints with information they have not thought of before. Furthermore, team members might see the benefit of evaluating alternatives and of taking a broader approach to decision-making. Hayashi (2004), for instance, found that teams whose members share and exchange knowledge tend to perform better. Furthermore, results of empirical research regarding the effect of task conflict on performance outcomes have proven that this type of conflict is generally beneficial. Task conflict is productive in groups performing non-routine tasks (Jehn 1995) and it enhances the quality of decisions (Amason 1996, Pelled et.al., 1999). Based on this evidence, we advance the following proposition:

Proposition 6 : debate will be positively related to board task performance

5.5 Limitations and boundary conditions of the model

The model we have developed is characterized by several limitations and boundary conditions. Caution is also required in empirical testing. First, the model that we propose is primarily developed for one-tier or unitary boards. Although the unitary board of directors is internationally the most prevalent, it must be noted that some European countries have a two-tier board structure, for example Germany, the Netherlands, Denmark etc. As both systems are grounded in varying legal and historical contexts, it is

clear that a unitary and a two-tier board differ substantially in their composition, operations and responsibilities (see Chapter 2). We contend that these differences should be taken into account when exploring board processes and consequently determining the effectiveness of boards.

Second, the theoretical model has been developed in the wake of our extensive field study. The qualitative empirical findings were compared and complemented with additional sources in order to extract process variables that we believe were the most relevant for the effectiveness of boards of directors. In particular, we have distinguished three intervening variables, namely cohesiveness, debate and conflict norms. However, a variety of other process variables exist that have been identified in (group) literature but that are not included in our board model. Examples are internal task process (Ancona and Caldwell, 1992), use of knowledge and skills (Forbes and Milliken, 1999), decision-making attention (Golden and Zajac, 2001) and decision comprehensiveness (Simons et.al., 1999). Nevertheless, they also offer interesting avenues for further research, particularly from the angle of the decision-making process. It might be worthwhile to explore to what extent these variables contribute to our model of board effectiveness next to the ones that we have selected.

Third, although we have supported the proposed relationships with evidence from both the corporate governance literature and literature on group effectiveness, they are not exclusive. In spite of the fact that the identified intervening variables are separate constructs, we acknowledge the possibility that they can influence each other. For example, when board members air their ideas in open discussions, the danger of groupthink diminishes. Conversely, boards that are more fragmented, may be hampered in conveying debate, and directors feel less motivated to make an effort to contribute. In addition, it can be stated that not all of the relationships may be one-directional and for instance, board outcomes reciprocally impact board structure. When the strategic or monitoring tasks are not carried out in a sufficient manner, the board will likely decide to change the composition of the board. Still, it is more difficult to predict the exact nature and strength of these relationships amongst the variables.

Fourth, it must be noted that the static nature of input-process-output models of group effectiveness has raised critical questions, and there is a plea to pay more attention to the dynamic nature of group systems (Ruigrok and Tacheva, 2004). Demb and Neubauer (1992) already touched upon this issue by introducing the “reinforcing loop” in order to conceptualize the findings of their directors’ poll. Although we value their approach, mapping board models that way, it is not evident to detect the determining variable that reinforces either positive or negative cycles of board behaviour. Perhaps longitudinal research methods may shed more light on this interdependence nature of dynamic board systems.

Fifth, in our model, board effectiveness has been defined as a dual role set, supported by the underlying theories. However, as the theoretical foundations simultaneously provide complementary and conflicting propositions on the role and responsibilities of the board of directors, a question arises as to their varying usefulness. Lynall et.al. (2003), for example, stated that “it is not a matter of choosing one theoretical perspective over another but, rather, of identifying under which conditions each is more applicable” (419). A first attempt to identify the conditions which determine the extent the board prefers one role to another is covered by Zald (1969). In his paper he points to four factors (i) structure of external groups (e.g. concentrated ownership), (ii) dependence of the company on its directors, especially the need for financial support, (iii) the directors’ knowledge of the company’s operations, and (iv) the general health and conditions of the company (e.g. crises and transitions). Building on the work of Zald, Zahra and Pearce (1989) identify additional internal and external contingencies such as company size and life cycle, type of business, CEO style, industry type etc.

Finally, some researchers strongly plea to incorporate such a contingency perspective in board research in a more substantial way (Nicholson and Kiel, 2004b; Heracleous, 2000). In fact, these researchers advocate the idea that a company should tailor its governance structures and processes to its environment. Previous research on high-tech, venture-backed companies for instance, has already revealed how governance structures and processes differ from more traditional companies (Van den Berghe and Levrau, 2002). As

a consequence, it can be stated that specific board attributes that are beneficial for one company may turn out to be detrimental to another. The contingency perspective might be of particular relevance when testing our model for board effectiveness on different types of firms.

5.6 Conclusion

In this chapter we have pointed out that research on boards of directors has traditionally been focusing on a direct link between board characteristics and firm performance, while ignoring potential intervening variables. Recently, a handful of scholars have tried to fill this void by proposing process-oriented board models as an indirect route. We rely on this stream of research by presenting a new theoretical research framework for evaluating the effectiveness of boards. In fact, our model develops a rationale to explain how specific board processes may influence board outcomes which in turn may affect corporate performance. In developing our model we have integrated the corporate governance literature with literature on group effectiveness. While there is an extensive amount of research on boards and a large body of work on group effectiveness, very few integrative studies can be found. Supported by the qualitative findings of our preparatory field study, we extract the significant variables from the separated literature and integrate them into a theoretical model of board effectiveness. Relying on the input-process-output approach, we have explored variables that we believe are critical in determining the effectiveness of boards. We go beyond the structural characteristics of boards of directors to also include behavioural or attitudinal measures of board effectiveness. We have argued that cohesiveness, debate and conflict norms may be intervening variables which mediate the relationships between board input and board outcomes. In doing this, we have tried to clarify the inconsistent results found in empirical research on boards. Furthermore, specific relationships have been proposed. Empirical research is required to confirm the model and to validate the proposed relationships. We believe this kind of research may help to explain the differences between successful boards and board failures.

5.7 References

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6 Board effectiveness in practice: a case study

6.1 Introduction

Chapter 5 provides the theoretical framework for the second part of our empirical research. In particular, we have developed a process-oriented model for board effectiveness that pays attention to potential intervening variables between board characteristics (input) and board performance (output). Moreover, we have presented several propositions which express relationships between the variables. At the heart of the model is the belief that the interactions and relationships amongst board members determine to a large extent the collective outcomes of the board of directors. In fact, the model suggests that behavioural or attitudinal aspects of boards represent the catalyst that unlocks (or locks) the potential - provided by structural aspects - for boards to be effective in fulfilling their roles.

In this chapter, we present the case of a major Belgian listed company (the Company) that we studied at the end of 2005. The case study is used to evaluate and validate the theoretical research model. The Company's board of directors constitutes an interesting example to examine the intangible aspects that contribute to the effectiveness of boards. It does not only provide the unique opportunity of studying a high elite class whose accessibility is uncommon but it also leads to a better understanding of how board effectiveness is shaped by a complex web of factors.

This chapter is structured as follows. First, we explain the outlines of the theoretical research framework. The latter provides the background for the case study. Next, we discuss the research methods that were followed during the field study. Section 3 of this chapter includes a brief description of the Company's sector, mission, activities and governance structure. This description allows a better understanding of the context in terms of the strategic and governance challenges the Company faces. In section 4, we evaluate the robustness of our board model which we have developed in the previous

chapter. In particular, by combining both qualitative and quantitative data, we assess the nature of the relationships between the predefined variables. Finally, the findings are used to reconsider our research model and to draw conclusions.

6.2 Background

The board of directors, as the ultimate decision-making body, is assumed to add value to an organization. However, despite the intense interest in boards of directors, our understanding of how boards contribute to organizational performance is still relatively undeveloped (Nicholson and Kiel, 2004(a)). In Chapter 4, we have documented that a great deal of literature on boards of directors has traditionally been centred around direct board-performance links using organisational performance (e.g. Dalton et.al., 1998) or critical decisions (such as greenmail (Kosnik, 1990) or CEO turnover and remuneration (Core et.al. 1999; Weisbach, 1988)) as dependent variables. It was noted that decades of research have enhanced our insights on boards of directors, but at the same time no solid evidence is provided on how and to what extent boards of directors add value to their companies. Moreover, it was argued that mainstream board research has relied on incomplete models which largely ignore the influence of various intervening variables between board inputs and performance outputs. In fact, Tricker's (1978) observation that the work of directors, in and out of the boardroom, is rated as the most under researched management topic, is still much alive. In this respect, Hermalin and Weisbach (2000) have contended to establish a new research direction which should unfold along three lines: (i) modelling of the inner workings of the boards; (ii) tests of the implication of particular models and (iii) studying boards of organizations other than the largest-publicly traded corporations. Although recent work has followed one or two approaches (behavioural board model by e.g. Huse, 2005; empirical study of board effectiveness in non-profit organisations by e.g. Cornforth, 2005 and 2001)), we believe that subsequent work in these three main directions will continue to add much to our knowledge on boards.

Understanding how boards actually work is not an easy task and requires a range of tools (Nicholson and Kiel, 2004(b)). Modelling or developing a conceptual framework is considered to be a key tool, because it indicates how factors are related to each other and/or how factors can cause changes to others. Notwithstanding the abstract nature of frameworks and models, it is important that reality is adequately reflected (Sutton and Staw, 1995). Based on the empirical findings of our exploratory field study (see Chapter 4), we have developed a conceptual model for analyzing board effectiveness (we refer to Chapter 5 for a more detailed description). Our model, which basically follows an input-process-output approach, has three main characteristics. First, board effectiveness (the output variable) is defined in relation to *the tasks the board of directors* is expected to perform. In particular, we have approached an effective board as one that can successfully execute *a dual role set*, namely its strategic and monitoring role. Literature, in contrast, has traditionally focused on the board's execution of a single role rather than on an integrated role set (Nicholson and Kiel, 2004(a); Hillman and Dalziel, 2003). In addition, due to the dominant reliance on agency theory in corporate governance and board research, literature has (over)emphasized the monitoring and control functions of the board at the expense of other functions, such as strategic or resource dependence roles (e.g. Johnson et.al., 1996). Both tendencies have resulted in an incomplete understanding of what boards actually do.

Second, emphasis is placed on *board processes* in addition to the size and composition of the board as factors influencing board effectiveness. In particular, we have identified three intervening variables (cohesiveness, debate and conflict norms) which we believe mediate the effects of board structural characteristics on board task performance. The bulk of research on boards has focused too much on structural factors and only recently has a more behavioural perspective (in terms of a focus on the working relationships amongst board members) in board research started receiving increased attention (e.g. Nadler et.al, 2006; Huse, 2005; Roberts et.al., 2005, Toshi et.al., 2003; Sonnenfeld, 2002). In particular, this research makes a strong case for the fact that board composition (as a proxy) can not replace the behaviours of board members in determining the effectiveness of the board in pursuing company success. From this perspective, it is

crucial to get a better picture of the inner workings of a board of directors as well as to enhance the knowledge on the relationships between board members.

Third, the concept of *board diversity* is introduced as an additional input variable. Despite the huge interest in other research settings, the issue of diversity has been - to a large extent - unexplored in the contexts of boards (Carter et.al., 2002). In fact, the overwhelming emphasis on agency theory in board research has led to the dominant assumption that board effectiveness is a function of a board's independence from management. As a consequence, much attention in literature is paid to the ratio and role of outside, independent directors (Walsh and Seward, 1990). From an agency perspective, the concept of diversity has not been of a concern. In contrast, the value of board diversity is recognised by resource dependency theorists (e.g. Pfeffer and Salancik, 1978) who touch upon diversity as a means for providing critical resources (legitimacy, advice and counsel, channels of communication and tangible resources). However, the issue only received moderate support in empirical board research.

In line with the view of Hermalin and Weisbach (2000), a next step to enhance our understanding of boards is the validation of our model. In order to do so, we have opted for a case study of a Belgian listed company, active in a high velocity environment.

6.3 Research design

The main research question that is addressed in the second empirical field study is “how do board processes influence the task performance of boards of directors”. By developing a process-oriented board model, we have approached this research question from a theoretical point of view. In particular, we have documented how different structural and ‘intangible’ variables are interconnected to form an integrated set of criteria which influence board effectiveness. Moreover we have expressed our expectations of relationships amongst the identified variables. By means of an empirical field study, we will evaluate and validate the robustness of our theoretical research framework.

6.3.1 *Case study method*

We chose to study board effectiveness in a natural setting by investigating the board of directors of a Belgian listed company. The choice of a single case is supported by Yen (2003, 1994) when (i) an investigator has an opportunity to observe and analyze a phenomenon previously inaccessible to scientific investigation or (ii) when the case represents the critical case in validating a clear set of propositions derived from theory. Both arguments are applicable to our study. We refer to Chapter 3 for a more detailed explanation on case study as a research strategy.

Quality measures. A major challenge in case study research is to ensure that data collection and data analysis meet tests of reliability, construct validity, external and internal validity (Yin, 2003). We promoted reliability (1) by using a case study protocol in which all informants were subjected to the same interview questions, and (2) by creating a data base to organize the interview notes and other documents. Construct validity was enhanced (1) by using multiple sources of evidence (data triangulation), (2) by establishing a clear link between empirical data and theory and (3) by a verification of the case study report by the board members who checked the truthfulness and accuracy of the information reported. External validity is limited to generalizability of the findings to theoretical proposition rather than populations. Finally, we addressed internal validity (1) by investor triangulation and (2) by the "pattern matching" analysis method described by Yin (2003). We refer to Chapter 3 for a more detailed description on the limitations of case study research.

6.3.2 *Sources of information*

We obtained our empirical data by relying on three data resources : (1) semi-structured interviews with all board members, (2) a written questionnaire, and (3) documentation.

Interviews with all board members. We conducted face-to-face focused interviews which typically lasted for one to one and a half hours, but occasionally took as long as

three hours. Each interview consisted of three major parts. In a first part, we gained a general impression on how directors perceived the effectiveness of the Company's board of directors. In a second part, we probed for the different factors which influence board effectiveness, using a standard set of questions. A third part included questions for clarification and verification of responses in the written questionnaire. Each interview was conducted by an interview team and additional rules were followed for within-case analysis. We refer to Chapter 3 for a more detailed explanation.

Questionnaire. We also obtained quantitative data from written questionnaires, which board members filled out before the start of the interview. The questionnaire covered a broad range of board issues and included measures for the variables within our theoretical research framework. We refer to Chapter 3 for a more detailed description of the questionnaire and to Chapter 5 for an explanation of how we measure the constructs in our board model.

Documentation. Additional information was gathered by means of primary and secondary documents, such as the Company's annual report, charters, relevant laws and regulations etc. We refer to Chapter 3 for a more detailed explanation regarding the use of documentation as a source of evidence.

6.4 Presentation of the case study

6.4.1 *The Company's environment*

The Company in our study operates within the telecom sector. This sector can be characterized as a **high velocity industry**. The latter is characterised by a rapid and discontinuous change in regulation, technology, competitors and demand (Bourgeois and Eisenhardt, 1988). In essence, we can identify four forces at work which have had a major impact on the telecom sector over the past two decades, and which are expected to influence the industry over the next years. First, the European Commission pushed for a *broad liberalisation* of the telecom sector in order to generate more competition, better prices and services for the consumer. In this respect, different regulations have been

revised and have changed the competitive landscape, also in Belgium. Second, the sector faces a strong *technological evolution*. This evolution materialises itself in terms of new applications, changes in transport media and in infrastructure. Companies have started to bundle different communication and entertainment services such as telephony, internet and television (defined as “triple play”). Third, there seems to be *consolidation* amongst existing players and emergence of *new and diverse players*. In Europe and in Belgium too, the telecom incumbents have preserved a leadership position, but new competitors have entered the market. In contrast, North America is confronted with many mergers and acquisitions leading to the emergence of a few large players. Fourth, *customer demand and behaviour* is rapidly changing. In general, customers are becoming more technology savvy and more demanding, in particular regarding integrated solutions.

6.4.2 *The Company’s mission, strategy and activities*

In a few years time, the Company has evolved from a classic telephone company to a full telecommunications company. The technological revolution, especially, is creating new opportunities which force the Company to keep up with recent developments in the field of communication . This is reflected in its vision and resulting mission.

Vision : The Company believes in a world where unlimited communication possibilities will create new unexpected services of uplifting benefit for all.

Mission : By opening up the amazing universe of communication possibilities, the Company enables and inspires people and organizations to achieve their dreams and goals in their ever changing world.

(annual report, 2005)

Box 1: The Company’s vision and mission

At the Company, **strategy** is defined in a **long-term context** and revolves around **three pillars**: operational excellence, maintaining market leadership for the core activities, and the pursuit of new development opportunities. The strategic goals are referred to as BELG (annual report, 2005):

B for “Become Best-in-Class”: this reflects the Company’s overall purpose and its desire to maintain its number one position in Belgium and ranking amongst the most efficient operators in Europe. To achieve this objective, three principles must be followed:

E for “Excellence”: meaning that the Company wants to make excellence a priority with respect to (i) managing costs, human resources, and technical know-how, (ii) synergizing activities within the Group and (iii) customer interactions.

L for “Lead”: meaning that the Company continuously strives to (i) maintain its leadership position in Belgium in the area of voice telephony, by launching new products and services, (ii) play a pivotal role in the triple-play market by promoting its network, ADSL and digital TV and (iii) to build customer intimacy by offering a range of innovative products.

G for “Grow”: meaning the Company must (i) expand in the data and e-services markets, (ii) pursue international growth through its carrier subsidiary and (iii) extend its activities beyond Belgium, in both fixed-line and mobile telephony markets.

The core activities of the Company are split up in **three business unites**: Fixed Line Service (FLS), Mobile Communications Services (MCS) and International Carrier Services (ICS).

Fixed Line Services. The Company offers a comprehensive range of voice, data transmission and internet services over the fixed telephone line for both professional and residential customers. At the end of 2005, the Company counted approximately 5,2 million *access channels* to its fixed-line network (PSTN lines, ISDN lines and ADSL retail). Besides, being Belgium’s main Internet Service Provider (ISP), the Company provides *narrow- and broadband Internet access* to over one million subscribers. The Company is also the leading provider of *data connectivity* services in Belgium where it offers a range of enterprise data site-to-site and user-to-site services which can be tailored to business customers' requirements. During 2005, the Company branched out into the *digital television sector*, launching digital TV in June. At the end of 2006 more than 100.000 Belgians subscribed to digital TV.

Mobile Communications Services. The Company is the main provider of mobile communication in Belgium. The major brand has 4,25 million active customers and offers a broad range of mobile communications services, including traditional voice, data (SMS, MMS), a large range of mobile solutions for companies and roaming services, as well as wholesale data services to third-parties

International Carrier Services. These activities are carried out by the company's subsidiary 'International Carrier Services'. In 2005, the latter combined forces with a foreign Carrier Services in a joint venture. The subsidiary 'International Carrier Services' is the preferred supplier of international connectivity services to the two partners involved and provides voice and data capacity and connectivity services to other telecommunications operators around the globe.

In Belgium, the Company (including its subsidiaries) is **a market leader** in many fields, particularly in wholesale and retail fixed line services, mobile communications, Internet and broadband data transmission services.

6.4.3 The Company's financial position

The Company has a strong and **sound financial position** as illustrated by Table 21.

Table 21: key financial figures of the Company

	<i>Before</i>		
	<i>IPO</i>		<i>After IPO</i>
	2003	2004	2005
Income Statement (in EUR million)			
Total revenue before non-recurring items	5,454	5,540	5,458
EBITDA* before non-recurring items	2,250	2,394	2,214
Net income (Group share)	172	922	959
Cash Flow Capital Expenditures (in EUR million)			
Cash flow from operating activities	296	1,899	1,883
Capital expenditures	(502)	(556)	(696)

Balance sheet (in EUR million)			
Balance sheet total	6,009	5,368	5,831
Net financial position	157	110	534
Data per share			
*Earnings Before Interests, Taxes, Depreciation and Amortization.			

(Source: the Company's website, investors' corner)

Since the IPO in March 2004 the Company's shares have been listed on the Euronext Brussels Stock Exchange and have been included in a total of 53 indexes, amongst which are the BEL20 (main Belgian caps) and the major European/telecom indexes. Table 22 below shows the main indicators on the Company share performance.

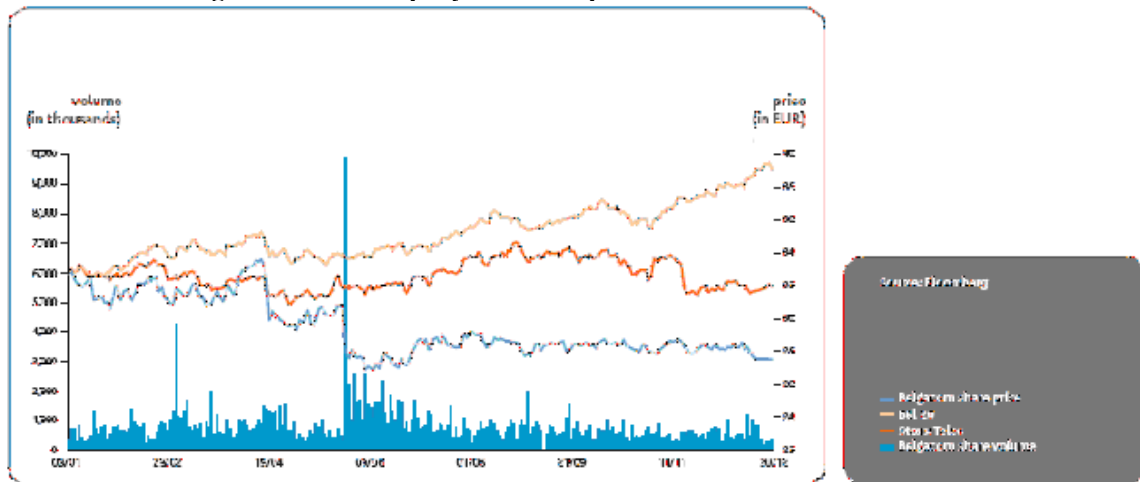
Table 22: key figures on share performance

	2004	2005
Market capitalization 31 Dec. (in EUR billion)	11.15	9.38
Data per share		
Basic earnings per share (in EUR)	2.57	2.78
Dividend per share, gross (in EUR)	1.38	1.52
Price/Earnings ratio 31 December	12.36	2.36

(Source: annual report 2005)

In 2005, the company share price was under considerable pressure in the first half of the year but managed to remain fairly stable over the second half. The share, however, underperformed the Telecom sector-index and the BEL20-index (see Figure 13).

Figure 13: the Company share compared to BEL20 and Euro STOKX



6.4.4 The company's governance structure

The Company's corporate governance model is to a large extent influenced by its specific legal status as well as by the recommendations of the Belgian Corporate Governance Code (Lippens Code). As a limited liability company under public law, the Company is in line with the law of 21 March 1991 reforming certain public economic enterprises. For matters not explicitly regulated by the 1991 Law, the Company is governed by the Belgian Company Code. Being just listed on the Euronext Stock Exchange, the Company fully complies with the requirements of the Lippens Code. This regulatory framework shapes the context of the relationships between the different actors in the corporate governance tripod (see Appendix 6).

6.4.4.1 Shareholder structure

In general terms, the shareholder structure has not substantially changed since the IPO in 2004 (see Table 23). Before the IPO, the shares were mainly distributed between a Belgian majority shareholder and an international private consortium. After the IPO, the major shareholder kept its stake in the Company while the private consortium sold its shares to the public.

Table 23: the Company's shareholder structure

<i>Situation on 31/12/2003</i>	<i>% in total</i>	<i>Situation on 31/12/2005</i>	<i>Shares</i>	<i>% in total</i>	<i>% voting rights</i>
Majority shareholder	50,0%	Majority shareholder	180.887.569	50,00%	53,14%
Private consortium	46,9%	Free-float*	157.525.777	43,54%	46,28%
The Company (own shares)	3,1%	The Company (own shares)	21.380.565	5,91%	0,00%
		Personnel	1.981.224	0,55%	0,58%
		Total	361.775.135	100,00%	100,00%

(Sources: annual reports 2003, 2005)

* In accordance with the Belgian Transparency Law, holdings of 5% (or a multiple of 5%) of the total share capital must be declared to both the BFIC (Banking, Finance and Insurance Commission) and the company itself. The Company's articles of association have reduced this threshold to 3%. In this context, an institutional investor (Belgian investment fund) reported that it had acquired a shareholding of more than 3%.

From this point of view, the Company can be considered to be a **closely held listed company, controlled by a major shareholder**, holding a large part of the shares. Chapter 2 provides some descriptive statistics on ownership concentration in Belgium. In particular, it is indicated that 80% of Belgian listed companies have a major shareholder who controls the company either directly (participation > 50%) or indirectly (participation between 25% and 50%, and in control through formation of coalitions through voting pacts or similar arrangements). In this respect, the Company's shareholder structure resembles that of an average Belgian listed company.

6.4.4.2 Board of directors

6.4.4.2.1 The composition of the board of directors

The board of directors of the Company is composed of maximum 18 members, including the Chief Executive Officer (CEO). There are two distinctive features with respect to the composition of the Company's board of directors: appointment of directors and language parity (the Company's Articles of Association, 16 and 18).

First, the board of directors consists, besides the CEO, of two broad categories of non-executive directors:

- (i) Board members who are appointed directly by the majority shareholder, in proportion to the number of votes held. They are considered as the non-executive directors representing the dominant shareholder.
- (ii) Board members who are appointed in the General Meeting of Shareholders, and by a separate vote amongst the other shareholders for the remaining seats. These board members are appointed solely from a list of candidates proposed by the board of directors. In accordance with the Belgian Companies Code, at least three board members must be independent in line with the legal definition. However, the Company is striving for a proportion of 50% independent directors.

Second, in constituting a board of directors, the Company must take language parity into account. The latter means that the same number of French-speaking members and Dutch-speaking members must sit on the board of directors, with the possible exception of the chairman of that board. Board members who are neither French-speaking nor Dutch-speaking are not taken into account in determining the linguistic parity.

Both requirements also have implications regarding the positions of chairman and CEO (the Company's Articles of Association, 19 and 20). The Company has separated the roles of chairman and CEO. Both the chairman of the board of directors and the CEO are appointed by the major shareholder and must belong to different language groups.

Table 24 presents the composition of the Company's board of directors at the end of 2005.

Table 24: composition of the Company's board of directors

<i>Name</i>	<i>Category</i>	<i>Directors since</i>	<i>Term expires</i>	<i>Language</i>	<i>Gender</i>	<i>Age</i>
Director A	executive	2003	01/03/2009	F	Male	50
Director B	NED-MS*	2004	01/03/2009	N	Male	52
Director C	NED-MS	1994	23/12/2006	N	Male	54
Director D	NED-MS	1996	23/12/2006	N	Male	39
Director E	NED-MS	1994	23/12/2006	F	Female	55
Director F	NED-MS	1994	23/12/2006	F	Male	57
Director G	NED-MS	2003	30/09/2009	F	Male	59
Director H	NED-MS	1994	23/12/2006	N	Male	59
Director I	NED-MS	1994	23/12/2006	N	Male	52
Director J	independent	2004	AGM 2010	F	Male	61
Director K	independent	2004	31/12/2006	F	Female	45
Director L	independent	2004	AGM 2010	E	Male	51
Director M	independent	2004	31/12/2006	F	Male	65
Director N	independent	2004	31/12/2006	N	Male	62
Director O	independent	2004	31/12/2006	E	Male	63
Director P	independent	2004	31/12/2006	N	Male	52
Director Q	independent	2004	AGM 2010	N	Female	53
<i>One vacancy**</i>	<i>independent</i>					

(Source: annual report 2005)

* NED-MS denotes non-executive directors representing the major shareholder

** the vacancy for one independent director has not been filled after the departure of director

Some observations can be drawn from this table. First, it is clear that the current board of directors is *recently appointed*. In fact, the IPO resulted in a renewed composition of the board of directors. Fully in line with the corporate governance recommendations, new independent board members were appointed by proposal of the board. They replaced the members who had represented the private shareholder consortium and who ceased to be shareholders when the Company became listed on the stock exchange. In fact, with the exception of the CEO, the board of directors is composed of *50% independent directors*.

Second, the *size of the board is quite large*. In fact, the maximum number of directors, as laid down by law and the company's Articles of Association, has not changed since the

IPO. The actual board size is the result of a respect for equilibriums, as the Company is required to keep certain balances (language parity, shareholder representation versus independency etc.). In addition, board size is intended to be large enough in order to include sufficient members who are expected to contribute experience and knowledge from different fields.

Third, the composition of the board reflects *the desired diversity* in terms of age, gender and nationality.

6.4.4.2.2 Board committees

As recommended by many corporate governance codes, the board of directors has set up special committees. These include an Audit and Compliance Committee, a Nomination and Remuneration Committee and a Strategic and Business Development Committee:

- The *Audit and Compliance Committee* must include a majority of independent board members. The chairman must also be an independent board member. The Audit and Compliance Committee is currently made up of three independent directors (including the Committee's chairman) and two shareholder representatives.
- The *Nomination and Remuneration Committee* must be comprised of at least four board members and is currently made up of two independent directors and two shareholder representatives. The chairman of the board chairs this Committee.
- The *Strategic and Business Development Committee* must consist of a majority of board members representing the major shareholder. The Committee is chaired by the Chairman of the board of directors, with the CEO participating as an ex officio member. The Committee is currently made up of four members.

6.4.4.2.3 Comparison with an average board of directors of Belgian listed companies

The descriptives reveal some **similarities** between the Company's board of directors and an average board of directors of a Belgian listed company (as described in Chapter 2). First, a separated board leadership structure is a common practice amongst listed companies in Belgium. Second, most boards of directors of Belgian listed companies include a mix of executive, non-executive and independent directors. Third, the installation of board committees is commonly found amongst listed companies in Belgium. It is noted that these governance practices are to a large extent influenced by the recommendation of the Lippens Code and a willingness of Belgian listed companies to comply with the required standards of corporate governance.

In contrast, there are some **particularities** with respect to the Company's board of directors in terms of (i) exclusive rights of the major shareholder to appoint a certain number of board members, including the Chairman and the CEO, (ii) recent nomination of 50% independent directors, (iii) the large board size, and (iv) the installation of a strategic committee. Although these governance practices are not unique, they are less commonly found amongst Belgian listed companies.

6.4.4.3 Management

A **Chief Executive Officer (CEO)** is responsible for the day-to-day management of the Company. To assist the CEO in the performance of his duties a **Management Committee** has been installed. The CEO chairs the Management Committee. At the time of the study, the Management Committee was made up of seven members. Besides the CEO, the Chief Financial Officer, Chief Strategy Officer, Chief Human Resources Officer and the 3 Officers leading the three business units, sat on the Management Committee.

6.4.4.4 Supervision and control

As with any other Belgian listed company, the Company is subject to external audit. The *financial supervision* which encompasses the auditing of the financial situation, the annual accounts and the regularity of the transactions recorded in the annual accounts is entrusted to a four-member panel of auditors. Two commissioners are appointed by the Court of Auditors. The others are appointed at the General Meeting from the members of the Institute of Company Auditors.

Particular for the Company is an additional *administrative oversight* exercised by a Government Commissioner, appointed and dismissed by the Crown. The role of the Government Commissioner is to ensure compliance with the law, the Articles of Association and the Management Contract. He must ensure that the Company's policy does not prejudice the performance of the company's public service obligations. In order to do so, the Government Commissioner is invited to all meetings of the board of directors and the Management Committee, where he participates in an advisory capacity.

6.4.5 Concluding remarks

Since the beginning of the nineties, the Company has faced important challenges with respect to both its strategic positioning and its governance structure. The environment in which the Company operates has been subject to a relatively high rate of change. The technological (r)evolution and the liberalisation/deregulation push at the EU level have enabled new possibilities for the traditional telecom operators while at the same time confronting them with increased competitive pressures. All of this has had important implications for the Company and in order to face this evolution the Company has restructured several times. These restructuring operations have drastically changed the Company's corporate structure, strategy, culture and image. Besides, in order to adjust to the changing environment, the Company's governance structure has evolved as well. In

particular, the board of directors has been adjusted to fit the new challenges and to be in line with the highest corporate governance standards.

From a governance point of view, the Company shows important similarities with the majority of other Belgian companies quoted on the stock exchange. In addition, the Company faces some distinctive governance features which may impose additional challenges on the effectiveness of its governance model in general, and of its board of directors in particular.

6.5 Analysis of the relationships between the determinants of board effectiveness

The research framework, briefly outlined above and presented in detail in Chapter 5, will be analyzed in terms of each of the identified determinants of board effectiveness and the expected relationships between the determinants. Observations induced from the Company's board of directors are also used to introduce elements of a more elaborated and integrated perspective on the effectiveness of boards of directors.

6.5.1 Board task performance as output

Based on the underlying theoretical perspectives, we have extensively described the roles a board of directors is assumed to fulfil (see Chapter 5). In particular, supported by the findings of our first empirical field study (see Chapter 4) we have contended that the board of directors needs to perform a two-fold role. On the one hand, boards are expected to control and monitor the company and on the other hand they need to be involved in strategy. This dual role set is also supported by the Company's directors.

Example R3: The board has two essential functions; these are the strategic sounding board and the supervision of management. The strategic sounding role implies a long term vision and a global approach of business issues, customers etc. The monitoring role does not equal 'control' in the strict meaning of the word because thereby the board can rely on audit bodies and other regulatory bodies; monitoring implies challenging management on a regular basis....

Yet, it is acknowledged that the predominance of one role over the other can vary according to companies of different types (Forbes and Milliken, 1999). For example, for companies operating in turbulent environments, the strategic role of the board is predicted to be of particular importance. The rapidly changing environment provides significant opportunities for boards of directors to take important decisions on strategic issues that help the organization adapt to the new circumstances (Pearce and Zahra, 1992; Boulton, 1978). Taking into account the particularities of the Company's environment (high rate of change and strong external controls, see paragraph 6.4.1), we expect a *predominance of the strategic role* of the Company's board of directors over its monitoring tasks. Our view is supported by the Company's role definition of its board of directors. As expressed in law and the Articles of Association, the Company's board of directors has the (legal) power to perform all acts necessary or useful to achieve the Company's corporate objects, with the exception of those reserved to other bodies within the company. Responsibilities that are the exclusive power of the board and which can not be delegated are (i) the approval of the Management contract, (ii) establishing the business plan as well as the general policy and strategy and (iii) supervision of the CEO, particularly with regard to the execution of the Management contract. Within this legal framework, the Company has opted for a board of directors which, conceptually, strongly associates with the notion of a "working" board - notably a board that is strongly involved in the strategy of the company (briefing note, July 2005). By use of the written questionnaire, we have tried to get insight into the extent to which the board of directors actually performs its strategic tasks. We identified seven strategic functions and asked the directors how involved the board of directors was in each of the functions using a 5-point Likert type scale (ranging from 1 'no involvement' to 5 'strong involvement'). The results are presented in Table 25. The relatively high average scores indicate a strong involvement of the board of directors in strategy.

Table 25: role of the Company's board in strategy

	<i>Mean score</i>	<i>Std dev.</i>	<i>Min. Score</i>	<i>Max. score</i>
Definition of the company's mission, objectives and values	4,20	(1,21)	2	5
Decision on the delegation of powers and responsibilities	3,53	(1,41)	1	5
Decision on the allocation of resources (financial, HRM, etc.)	3,53	(0,99)	1	5
Approval of plans and budgets	4,60	(0,63)	3	5
Discussion on strategic options related to Mergers & Acquisitions	4,47	(1,12)	1	5
Approval of Mergers & Acquisitions	4,67	(0,82)	2	5
Decision on the strategic direction the company should take	4,53	(0,91)	2	5

In addition to this quantitative investigation, we used interview comments to verify the findings. The qualitative data retrieved during the interviews revealed a more nuanced picture. Although all board members recognize the important role the board of directors has to play in strategy, it is observed that the board's impact on major strategic decisions is rather relative. Especially in important files, the involvement of the full board of directors does not meet directors' expectations. Several directors noted:

R5: The impact of the board on strategy is relative, even when there exists the will to do well. This is because certain files are presented to the board too late while clearly specific engagements are already taken by management... we have then the impression that 'the stakes are done'.

R9: Certain important strategic files are settled on too short notice by the board.

R10: With respect to the timing, sometimes strategic files are submitted to the board too late compared to the facts or decisions.

R17: It appears to me that when the management train has departed, the board needs to run after (...) files are presented to the board in 'slices'.

An important observation that clearly explains the gap between board (strategic) role expectations and actual board (strategic) task performance is the existence of the Strategic and Business Development Committee. The Strategic and Business Development Committee's role is to assist and advise the board of directors on matters concerning the Company's general policy and strategy, as well as on major issues regarding its strategic development (annual report, 2005). In general, the establishment of board committees is one of the structural measures put forward by corporate governance reforms in order to enhance the effectiveness of boards (Van den Berghe and De Ridder,

1999). The rationale behind this recommendation is that committees allow board members to delve more deeply into specific issues, and develop a specialized understanding so that the board can accomplish more in a limited time (Carter and Lorsch, 2004). Still, board committees can involve risks or lead to unintended side-effects that seriously limit a board's capacity to do its job (Van den Berghe and De Ridder, 1999). We found that these benefits and risks are particularly applicable to the Company's Strategic and Business Development Committee (see Table 26). Several directors explained how this committee supports the board of directors in the execution of its strategic tasks. The most important explanations relate to (i) more efficient use of time due to the (large) size of the board; (ii) the need to prepare, elaborate and discuss files beforehand and (iii) the role of sounding board for management in developing the strategy. In contrast, the existence of this committee clearly affects the way the full board of directors is able to carry out its strategic tasks due to the perception of (i) information asymmetry and (ii) pre-cooking of files and hence the dilution of the role of the board. While responsibility for providing strategic direction is borne by the board of directors as a whole, the Strategic and Business Development Committee plays a prominent role in developing and selecting the Company's strategy (especially regarding mergers and acquisitions). The strong involvement of only a subgroup of the board in major strategic files implies that the majority of the directors are left out of important discussions which causes discrepancy between the expected engagement of the full board of directors and the actual performance. This finding is consistent with evidence of previous qualitative research on boards. Carter and Lorsch (2004), for instance noted that the creation of a strategic committee disconnects the committee from board members who do not serve on it and as such prohibits all directors from focusing on major issues.

Table 26: benefits and risks of the Strategic and Business Development Committee

Benefits			Risks and side-effects	
Efficient use of time of small number of directors	Preparatory in-depth-discussions	Sounding board for management	Information asymmetry	Dilution of the board's strategic role
<i>Examples</i>	<i>Examples</i>	<i>Examples</i>	<i>Examples</i>	<i>Examples</i>
Having a board of 18 members, it is important to have a strategic committee... one does not get involved in strategy with 18 people (R1).	The objective of the strategic committee is to simplify the files in order to prepare board decisions. This is of utmost importance in a company which faces a high level of complexity (R10).	The CEO looks into the strategy with support of the board. As a consequence, it is evident that some members are seriously engaged in strategy (R16).	The SBDC may cause a problem, because board members are not on the footing of equality (...) members who are not part of the committee do not have the same information (R8).	If the strategic committee presents an opinion or decision, it is my impression that the board can not oppose it. As such, the committee erodes the power of the board (R12).
Discussing some strategic issues in a brainstorming way with 18 members seems unlikely to be efficient (R14).	There is a definite role to be played by this committee in preparing the strategy and specific M&A dossiers (R2).	With a small number of directors, when properly used, it is of added value for management. It offers a greater interaction with management (R1).	We sometimes have the impression that there is an asymmetry of information between the members of this committee and the board. Committee members have a lead over the others (R5).	SBDC dilutes the role of the board (R7).
Because of the size, one cannot have real strategic discussions in the board, there can be strategic presentations but that is not the same (R12).	The strategic committee has an important role to play. It enables discussions and the ability to work on files more in-depth 'en petit comité' ... after all, discussing strategy requires time (R3).		Some directors feel second-rate and the committee's existence creates some distrust (R14).	There is no pre-cooking in this committee and there are no decisions being taken, unfortunately the perception in the board is different (R14).
Discussing strategy can not be done in a board with 18 members (R3).	The strategic committee fulfils a preparatory role, it assembles a small number of directors to discuss certain issues 'en petit comité' (R14).		SBDC generates a board within which two groups of directors work at different speeds. It gives different responsibilities to different members.. it is definitely not at the strategic level that differentiation of board members must exist... strategy is one of the most important roles of the board (R13).	

The written questionnaire also included questions regarding *the monitoring role of the board*. In order to get insight into the extent to which the board of directors actually performs its control functions, we identified five monitoring tasks. We asked the directors how involved the board of directors was in each of these tasks using a 5-point Likert type scale (ranging from 1 ‘no involvement’ to 5 ‘strong involvement’). The results are presented in Table 27. At first glance, the mean scores point to a rather moderate level of board involvement in monitoring.

Table 27: role of the Company's board in monitoring

	<i>Mean score</i>	<i>Std. dev.</i>	<i>Min. score</i>	<i>Max. score</i>
Monitoring of the results and implementation of the strategy	4,40	(0,99)	2	5
Monitoring of the company assets and their allocation	3,53	(1,19)	1	5
Monitoring of management	3,60	(1,35)	1	5
Monitoring of the presence and effectiveness of internal monitoring systems	3,47	(1,36)	1	5
Evaluation of risk management	3,33	(1,34)	1	5

Qualitative data gathered during the interviews helped to interpret these scores. In particular, the minimum scores need to be interpreted with care due to potential response bias. From the interviews, it became clear that some directors make a distinction between the tasks of the (full) board and the responsibilities of the audit committee. By consequence, the scores may underestimate the real involvement of the ‘board level’ in control tasks. The Company’s directors explained that the board can rely, in fulfilling its control duties, on (a) a well-functioning and competent Audit and Compliance Committee and (b) the well-developed internal and external control systems the Company has in place. These two conditions are perceived as fundamental for the board of directors in order to perform its monitoring role. According to the Company’s directors, the board’s monitoring role is in line with expectations and no real concerns are expressed.

Example R17: With respect to monitoring, the board is doing well; we have great trust in the competencies of the Audit and Compliance Committee and its chairman; in general very strong and structured control appliances exist within the Company.

The Audit and Compliance Committee plays an important role in ensuring the integrity of the Company's financial reports, the compliance with legal and regulatory requirements as well as in evaluating the risk framework and the methodology of risk assessment. In general, audit committees are considered one of the more powerful board committees as their main objective is to ensure the financial health of the company (Firstenbergh and Malkiel, 1994). Our findings highlight the importance of an audit committee for carrying out a board's monitoring role and are fully in line with the limited research on audit committees (Kesner, 1988; Daily, 1996).

Furthermore, the Company's board of directors as well as the Audit and Compliance Committee are supported by the Company's Compliance Office. The latter was set up in order to ensure that the activities of the Company - and of all its staff members - are carried out in line with the increasingly complex set of rules and legislations applicable to the Company's activities (annual report, 2005). In addition, the Company is subject to external financial and administrative oversight (see paragraph 6.4.4.4). Supported by this well-functioning control environment, actual board (control) task performance meets board (control) role expectations.

6.5.2 The key inputs: size and composition of the board

In the previous paragraph, we described how the Company's directors perceive the roles of the board of directors and to what extent the board actually performs these roles. In developing our theoretical research framework, we have identified three board characteristics which serve as structural input variables for the task performance of a board of directors. These are board size, board independence and board diversity. Board size and board independence are commonly recognized as key attributes by the various theoretical perspectives, while board diversity consistently received high scores during our first field study (see Chapter 4). Similarly, the majority of the Company's directors attach great importance to the competences of residing board members and value a complementary mix of expertise.

Examples R5: A mix of competences is a must to good decision-making.

R6: The assembly of competences and the quality of people is of utmost importance for a board of a company operating in an environment of rapid technological changes.

R10: Diversity amongst the people who sit at the boardroom table and their complementarity are crucial to arrive at good choices and good decisions.

At the end of 2005, the board of directors of the Company counted 17 members and compared to the average board size of a Belgian listed company, this number is quite large (see paragraph 6.4.4.2.3).

Half of the board members at the Company are considered to be independent. All the other members are non-executives except for the CEO (see paragraph 6.4.4.2.1). The 8 independent directors fully comply with the definition provided in the Belgian Company Code (annual report, 2005).

As explained in Chapter 5, diversity comes in many forms. Irrespective of the way they are labelled, in essence, there are two broad categories of diversity. The first category refers to differences amongst board members in overt, biological characteristics which are typically reflected in physical features. Such characteristics include age, sex, and race/ethnicity. A second category refers to differences in board members knowledge, skills, nationality, tenure, attitudes etc. and is less immediately observable. Table 28 presents some descriptive statistics on diversity regarding the Company's board of directors. The board composition with respect to age, gender, nationality and tenure is expressed in terms of the quantity of these characteristics, while the composition with respect to knowledge/skills is expressed in terms of the dispersion of that characteristic within the board.

Table 28: descriptive statistics on board diversity at the Company

<i>Visible demographic diversity</i>		<i>Informational demographic attributes</i>		
Age	Gender	Nationality	Knowledge/skills	Board tenure
	Female directors	Foreign directors		Mean = 4,5years
Mean = 55	Absolute number = 3	Absolute number = 2	Blau's Index	N≥2 years = 6/17
Min.39-Max.65	Ratio = 17,6%	Ratio = 11,8%		

Directors' age ranges from 39 to 65 and the average age is 55. The board of directors counts 3 female directors and 2 foreigners. Average board tenure reflects the number of years an individual serves on the board of directors (Johnson et.al., 1993). For the Company the average board tenure is 4,5 years and directors' tenure ranges from 1 to 11 years. 11 directors serve no longer than 2 years on the Company's board. We also developed a measure of board diversity that reflects differences in occupational or professional and educational background (Goodstein et. al. 1994, Kosnik, 1990). We first created four occupational groupings (CEO, former CEO, expert, financial representative) and five educational groupings based on the Company's directors' initial formation (economics, law, sociology, commercial engineer and civil engineer). Blau's index of heterogeneity was then computed based on the distribution of board members within these groups. Blau's index is defined as : $1 - \sum P_i^2$ where P_i represents the proportion of a board accounted for by the i th group. The index can vary from zero (indicating all board members are the same or complete homogenous) to a high of one (indicating all board members are different). With respect to occupational diversity the score is 0,74 while the score for educational diversity is 0,79. Both scores point to a *high degree of heterogeneity*.

6.5.3 Board processes: transforming inputs to output

Next to the structural board characteristics, we have introduced three process variables into our research framework namely debate, cohesiveness and conflict norms (see Chapter 5). The latter is considered as intervening variables which mediate the relationships between board (structural) characteristics and board task performance. In fact, we believe that these process variables are fundamental to transforming inputs into output. Hence, it is necessary to examine the different variables and how they interact to perform the transformation process.

6.5.3.1 The effects of board size and composition on debate

We approached debate as an open discussion of task-related differences and the advocacy, by different board members, of differing approaches to the board tasks (see Chapter 5). Defined this way, we assumed that debate expresses itself in a constructive manner and we expected that boards of directors expose different levels of debate. In fact, we contend that the expression of cognitive conflict is a crucial and beneficial component for board effectiveness. A board of directors can only make optimal use of its potential through an interaction process whereby board members provide and balance diverse perspectives to arrive at a decision. We quantitatively measured debate using a questionnaire item on the nature of discussions. The findings indicate that the majority of the Company's directors (70%) perceive the discussions during the board meetings as *constructive*. In addition, we asked the Company's directors to rate the level of debate that occurs using four items on a 5-point Likert type scale (see Table 29). The scale is commonly used in literature as a measure for debate (Simons et.al., 1999). We assume the scale value 3 to be the theoretical average. Cronbach's alpha for this four-item scale was 0,855. We first computed each individual's perception of debate and then averaged individual-level scores to obtain a board-level score. The average board-level score for debate is 3,52. We interpret this score as a '*moderate to high*' level of debate.

Table 29: level of debate

<i>Items</i>	<i>Debate</i>
When discussing an issue, clear disagreement is stated	Board-level score: Mean: 3,52 Std. dev. (0,75)
Different approaches are proposed to the issue	
Directors openly challenge each other's opinion	
Discussions of the issue become heated	

Of importance in this study, is the extent to which the nature and level of debate is influenced by the identified structural board input variables. In Chapter 5, we substantiated that the effects of board size and composition on debate are not unambiguous as they can be both positive and negative.

Positive effects. As board size can also be used as a proxy measure of directors' expertise (Zahra and Pearce, 1989), a positive effect on debate is expected when a board consists of a large number of board members. The availability of a large pool of expertise is assumed to produce more perspectives which contribute to the quality of board discussions. A similar positive relationship is expected between board independence and debate. Due to the absence of close ties to the CEO/management and the company, independent directors have the ability to engage in discussions in an unbiased and objective way (Van den Berghe and Baelden, 2005). In addition, independent directors are presumed to bring along important (external) information about business practices and policies thanks to their experiences in other boards. This facilitates discussion and enables problem-solving (Carpenter and Westphal, 2001). Finally, board diversity is also expected to positively influence debate due to the obvious reason that heterogeneous board members are likely to produce a broad range of solutions and decision criteria (Schweiger et.al., 1986). Heterogeneity is assumed to promote airing of different perspectives and to reduce the probability of narrow-mindedness (Kosnik, 1990).

Negative effects. In contrast, the group dynamics literature has shown that large groups encounter problems to conduct effective discussions due to communication, coordination and organization problems (Surowiecki, 2004; Hackman, 1990). Board largeness may inhibit effective participation by directors in board discussions. In this respect, group dynamic problems associated with large boards will negatively influence debate. A similar negative effect is expected when the board of directors becomes too diverse. The greater the diversity of board members, the greater the potential for conflicts and the likelihood of ineffective communication resulting from the lack of shared language (Golden and Zajac, 2001).

We qualitatively assessed the effects of size and composition by searching the interview data. The positive consequences of a large board for debate seem not so prevalent. Still, the advantage of the large board is perceived in terms of having a broader range of ideas at the board's disposal. As one director noted:

R7: Large boards are not cumbersome because they offer more diverse ideas.

The qualitative findings appear to be more convincing regarding the occurrence of specific group dynamic problems and their negative impact on debate. Many of the Company's directors commented that a large board of directors is difficult to coordinate, hereby hindering effective discussion and decision-making.

Examples R1: When an issue is discussed and decided upon in the board, it is important to evolve to coherence of the decisions. This coherence comes with fewer board members.

R12: The board is far too big to be effective. Consequently, the board falls into separate groups (...) with a smaller board it would be easier to focus the discussions.

R14: In fact, having too many members hinders good discussions.

In addition, it was noticed that a fraction of directors does not participate actively in discussions. This may indicate that the board does not fully draw on the potential of all its members. Our findings are consistent with evidence from previous qualitative research on boards. Carter and Lorsch (2004), for example, noted that there are often too many people in the boardroom to allow meaningful discussion, even if most of the board members are knowledgeable and ready to contribute. Large boards exacerbate the time constraints as there are too many people who need to be involved.

Also noteworthy are the findings regarding the impact of board independence on debate. In fact, the evidence is not straightforward. We expected that the detachment of independent directors from the daily business would bring a certain breadth and objectivity to the board discussions, however the empirical evidence points rather to difficulties in terms of the board's shortage of in-depth knowledge and understanding of the company or its industry. Put differently, it appears that it is not the issue of independence as such that makes a difference, but the competence and behaviour of directors in general. The use of expertise, the effort to learn about the business and the way directors establish their own credibility vary, and hence, influence their contribution during discussions.

Examples R1: A director must adapt himself to the environment in which he operates and try to understand the business, the social climate, the economic circumstances.... this is not always the casethere are members who are more experienced and more constructive than others.

R 7: (...) and diverging competences imply that the level of detail to deal with during discussions substantially varies.

R14: The competences in the board appear to be insufficient and that is for none of the parties interesting, nor for the board, nor for the CEO, nor for management.

The strong emphasis that is placed on the individual competence of board members, in order to have constructive and fruitful debate, has also been recognized in previous qualitative research. In essence, the contributions non-executive and independent directors can make in discussions are presumed to be functions of general and firm-specific knowledge as well as of the time they have available. For example, using evidence derived from approximately two hundred interviews with (Canadian) directors, Leblanc and Gillies (2005), noted that directors commonly assessed many of their peers, the outside directors in particular, as not sufficiently knowledgeable about the business to make major contributions to board decision-making. They argue that directors, in order to make a significant contribution, must have specific monitoring capabilities and some specific competencies relating to the strategy that the company is following. Demb and Neubauer (1992) have also pointed to the tension non-executive and independent board members face regarding the ability to bring in-depth understanding of the company and its industry setting, as well as perspectives from the broader business and socioeconomic environments, to the table. Apparently, the worldwide attention for board independence has surpassed the need for a set of directors who collectively have all the competencies that match the company's needs and hence will lead to good decision-making. Two additional observations may explain why we did not find strong evidence on the effects of board independence. First, true independence is difficult to define and to measure because much of what compromises independence can hardly be detected from the outside. The frequently advocated premise is that independence may be more a state of mind and depends largely on the individual director's involvement and the behaviour of that director inside the boardroom (Van den Berghe and Baelden, 2005). Second, the scarcest resource that many directors have is time. In this context, Goold (1996) documents the 10% versus 100% paradox and its applicability to boards of directors. The paradox refers to the (unrealistic) fact that boards in 10% or less of their time and energy should be able to improve on the decisions of competent executive management who are

devoting 100% of their time and energy to the business in question. The 10% versus 100% paradox suggests that the value-added interventions of non-executive and independent directors will only occur if they concentrate on issues where they can expect to contribute something that management lacks or overlooks. Both practices are difficult to trace from the outside and with the currently applied research methods.

Simultaneously, the same scholars argue that proper training programmes for non-executive and independent directors are a means to make these directors less ill-informed, and hence to enhance their effectiveness (Leblanc and Gillies, 2005; Goold, 1996). Although several Company's directors expressed concerns over their own level of knowledge, some value the education programmes provided by the Company in order to increase their understanding of the Company, its business, its products etc.

Examples R8: As a director, the distance between you and the company is quite big. To look at some issue in more depth increases the engagement of directors...

R9: A director must be prepared to inform himself and to take training courses regarding the activities and products of the company whose board he sits on; each mandate equals to study again.

R13: The company has provided training courses for the directors which is an interesting initiative.... In particular, it signals to management that the board is trying to inform itself to get to know the business.

Further findings were not very outspoken regarding the expected impact of board diversity on debate. Some empirical evidence was found in favour of the added value of appointing non-nationals to the board. It was noted that non-nationals bring a broader and more international view on the business and the company. They are more detached from the Belgian environment.

Example R1: Regarding the long term, the international vision is still insufficient, members are still too much Belgian oriented... attracting foreign directors, or directors with international experience are beneficial in this respect.

At the same time, the qualitative evidence points to negative implications stemming from communication problems. In particular, the appointment of non-nationals to the board has changed the working language which is perceived as an obstacle to some of the directors.

Example R14: Some directors are not master of the English language and it is difficult for them to express themselves. As a consequence, important nuances get lost during discussions which cause some frustrations and hindrances.

A possible explanation for the lack of strong evidence on the effects of different dimensions of board diversity is the general emphasis on directors' competences. As discussed above, the individual competence and the way this competence is used, are perceived to be more critical for the nature and level of debate than the degree of heterogeneity amongst board members. Another explanation relates to the applied research techniques. As previously indicated, written questionnaires as well as interviews have limitations in revealing the process of board deliberations. Other research techniques such as direct observations could shed more light on the extent to which discussions benefit from diverse perspectives and backgrounds. The findings by Curral et.al. (1999), for example, indicate that the activity level of board members in board deliberations varies according to their background and the topic discussed.

6.5.3.2 The moderating role of conflict norms

In chapter 5, we have suggested that conflict norms are a necessary condition for the emergence of debate. Conflict norms refer to standards that encourage an openness and acceptance of disagreement. We have argued that directors' behaviour and interaction are regulated by a set of informal and unwritten rules. As such, a board culture which stimulates open and candid discussions is assumed to be the extra element required to take full advantage of the potential provided by board size and composition. We quantitatively measured conflict norms using 5 items on a 5-point Likert type scale (see Table 30). In fact, the scale we used is an adapted version of a more extensive scale commonly recognized in literature as a measure for conflict norms (Jehn et.al., 1997). We assume the scale value 3 to be the theoretical average. The Cronbach's alpha for this scale was 0.688. We first computed each individual's perception of conflict norms and then averaged individual-level scores to obtain a board-level score. The average board-level score for conflict norms is 3,91. We interpret this score as *high conflict norms*.

Table 30: conflict norms in the boardroom

<i>Items</i>	<i>Conflict norms</i>
Critical questions are tolerated	Board-level score: Mean: 3,91 Std. dev. (0,36)
Differences in opinions are accepted	
Disagreement is dealt with openly in the board	
Disagreement is detrimental to getting the work done by the board*	
Directors try to avoid disagreement at all costs*	

* reverse-scored

The qualitative findings of the interviews corroborate the results of the written questionnaire and point in favour of a culture which permits the airing of opinions.

Examples R5: There exists an open, direct communication between the members; board members speak frankly, discussions are open (...) there exists a very open culture...

R13: There is a very good sphere at the table in spite of strong cultural differences! Open and rich board culture thanks to its diversity.

R14: There is sufficient disagreement but it is important that this open dynamic leads to something.

Although we found that the board is characterized by a high level of conflict norms and a willingness to challenge, we did not find strong direct evidence to what extent conflict norms affect the relationship(s) between board size, composition and debate. Still, we implicitly interpret the positive findings regarding the nature and level of debate (see paragraph 6.5.3.1) as a result of the existence of high standards of openness inside the boardroom. In fact, previous qualitative research on boards has already revealed that a board's set of norms, is a powerful driver of directors' behaviour. These norms tend to determine when it is appropriate to speak, how to intervene and which directors' opinions deserve respect. The ultimate goal is to foster high standards that encourage productive and open discussion as well as resolve conflicting opinions (Carter and Lorsch, 2004).

6.5.3.3 The effects of board size and composition on cohesiveness

The last process variable that was included into our research framework is cohesiveness (see Chapter 5). Cohesiveness is considered to be affective in nature and is defined as the

degree to which board members are attracted to each other and are motivated to stay on the board. We have contended that a minimum degree of cohesion amongst board members is required for a board of directors to operate as a collegial team. We quantitatively measured cohesiveness using 4 items on a 5-point Likert type scale (see Table 31). In fact, the scale we used is commonly recognized in literature as a measure for cohesiveness (O'Reilly et.al., 1989). We assume the scale value 3 to be the theoretical average. The Cronbach's alpha for this scale was 0.793. We first computed each individual's perception of cohesiveness and then averaged individual-level scores to obtain a board-level score. The average board-level score for cohesiveness is 3,66. We interpret this score as a *'moderate to high' level of cohesiveness*.

Table 31: cohesiveness amongst the board members

<i>Items</i>	<i>Cohesiveness</i>
The directors get along together very well	Board-level score: Mean: 3,66 Std. dev. (0,43)
The directors are ready to defend each other from criticism by outsiders	
The directors are ready to cooperate and help each other	
The directors really stick together	

Qualitative interview data supports the quantitative findings. A few Company's directors commented on their impression by stating that they experience at least a minimum degree of cohesiveness while some other Company's directors noted that the cohesiveness is (still) growing.

Examples R5: I hear no criticism against one or another and each member seems to act according to his own personal feeling and convictions.

R10: There are very diverse personalities...one may look at the members as belonging to the old and new wave but the actual situation is more propitious.

R12: Even when directors had strongly different views during meetings, they still got along quite well afterwards. That is very unusual.

R15: (...) the cohesiveness is growing. There are some new members on the board and the directors are getting to know each other better.

Of importance in this study, is the extent to which cohesiveness in the board is influenced by the identified structural board characteristics. In Chapter 5, we substantiated that board size and composition trigger negative effects on the cohesion amongst board members. In

particular, socio-psychological research on groups, suggests that board members may experience difficulties to establish the interpersonal relationships which further cohesiveness when board size is high (Shaw, 1976). A similar negative effect is expected from enhanced board independence. By definition, independent directors interact less frequently with each other and they are assumed to be less close-knit. Finally, social categorization and similarity/attraction theory provide the rationale for the proposed negative relationship between board diversity and cohesiveness. Heterogeneity in the board is expected to yield dissimilarity amongst board members which lowers interpersonal attraction and liking (Tajfel, 1982; Byrne, 1971).

We qualitatively assessed the effects of size and composition on cohesiveness by searching the interview data. We found that the coincidence of different factors related to the recent change in the board composition hamper the establishment of interpersonal relationships and inhibit a sense of connectedness amongst all board members (see Table 32). In particular, the simultaneous appointment of a large number of new independent directors impedes the ability to relate to each other and affects the interaction amongst board members. Our data also suggests that (the absence of) informal contacts influence the integration of (new) board members. The responses from the written questionnaire indicate that there are few informal contacts between the Company's directors outside the board meetings. This is reinforced in the interviews. Several Company's directors pointed out that there is little, or at least were not aware of any systematic contact amongst directors outside meetings. Moreover, they are in favour of being provided with opportunities to meet each other more frequently in an informal way, indicating a willingness to improve the team spirit. Finally, the integration of (new) board members seems to be affected by the size of the board. As one Company's director put it:

R8: The board is too big to get to know each other well.

Table 32: board independence, diversity and cohesiveness

<i>Board independence</i>		<i>Board diversity</i>
Importance of informal contacts		Importance of directors' tenure
<i>Examples</i>	<i>Questionnaire item</i>	<i>Examples</i>
Perhaps a yearly seminar, off site with management, could strengthen the feeling of belonging to the Company and reinforce the ties amongst the directors (R5).	The directors often socialize with each other off the job: 29% agree 24% disagree 47% undecided	The board is still 'young' members are not yet a team...(R2).
There are far too little opportunities to meet each other... tutorials are a good initiative but pure social events could also be organized (R4).		Some directors know each other quite well because they have served together for many years; the relationships are somewhat different regarding the new directors (R8).
It would be appropriate if the company creates the opportunity to get to know each other better (R8).		For now, the cohesiveness in the board is insufficient...new members have entered the board and it takes some time for the group to adapt (...) the relationship between some directors is mature due to other professional ties, but for now this is not the case with respect to the full board (R17).
More efforts should be made in improving relationships between the directors....(R17).		
The lunches before or after the board meetings are a good thing... a rotation scheme would make it even better as it gives directors the opportunity to get to know each other better (R14).		

Our findings regarding director's tenure are consistent with previous research on tenure heterogeneity in other settings. Research on work groups has suggested that both the average length of tenure in a group and the distribution of tenure amongst members are relevant to individual and group performance. In particular, studies have shown that homogeneity in the tenure distribution directly fosters their social integration because similarity in tenure facilitates group members' mutual attraction and interaction as they undergo similar experiences and develop common perspectives (O'Reilly et.al., 1989). In addition, the evidence on the effects of changes in board structure is also consistent with a phenomenon referred to as "cohort effects" (Hambrick and Mason, 1984; Pfeffer, 1983). The latter indicates that groups whose members are linked by a common date and share similar experience or history will think similarly about issues. Put differently, directors who joined a board at similar dates are more likely to interact and form cohorts.

6.5.3.4 The effects of debate and cohesiveness on board task performance

Debate and cohesiveness are suggested to influence the task performance of boards of directors. The effects of debate on the performance of the board's strategic and monitoring role are considered to be beneficial. In essence, the presence of debate provides a broader range of viewpoints, formalizes task-oriented disagreement and encourages critical evaluation (Eisenhardt et.al., 1997; Schweiger et.al., 1986). The effects of cohesiveness are less straightforward. It is argued that the accomplishment of complex and interactive tasks requires some level of interpersonal attraction to establish the required trust and respect amongst the board members. However, when the board becomes too cohesive, board members may face pressure to conform to group preferences at the expense of critical exploration of multiple alternatives during decision-making (Kosnik, 1990). We have used both quantitative and qualitative data to examine the relationships between debate, cohesiveness and board task performance. Table 33 summarizes the findings. Some support could be found in favour of a minimum level of coherence between the board members which positively contributes to the performance of the board's tasks. In addition, the results indicate that debate is beneficial and it was noted that decisions, in the end, are always made by consensus. Still, some comments suggested that there is room for improvement as the potential of debate is not yet fully used. As one Company's director put it:

R15: More effort should be made to reach a collective view in the board of directors. In some case, too many individual points of views are defended.

Moreover, it appears that the degree to which the board fulfils its strategic role may be hampered by the nature of the topics tackled during discussions. Both quantitative and qualitative data point out that sometimes the board of directors gets too engaged in operational issues and that too many details are discussed at board level. The interpretation of these findings is two-fold. First, we already observed that high emphasis was placed on the board's competences and concerns have been expressed about the gap between the board's available and required knowledge. This might explain why much time and effort is spent on details as the objective is to arrive at a similar level of

understanding. Second, consistent with previous qualitative research on boards (Robert et.al., 2005), non-executive and independent directors may fail to understand their essentially non-executive role. They face the major challenge of not seeking an executive role through over-involvement in executive decisions. The following comment by a Company's director illustrates this point of view:

R15: Directors themselves must understand their role and must keep in mind that they are not management but that they are there to fulfil a supporting role in creating shareholder value.

Table 33: debate, cohesiveness and board task performance

<i>Debate</i>		<i>Cohesiveness</i>	
<i>Questionnaire</i>	<i>Examples</i>	<i>Questionnaire</i>	<i>Examples</i>
Board-level score: 3,52	<p><u>Beneficial</u></p> <p>Even if the files are very complex, there is no formalism. Real debate is taking place; the board is not a body that ratifies (R10).</p> <p>There has always been the willingness to reach (as far as possible) a consensus of vote that prevents disagreement or disappointment when the decision is taken (R5).</p>	Board-level score: 3,66	<p>It appears to me that there is a great openness and the will to work together for the benefit of the company. The board members are motivated and there exists a desire to add value (R5).</p>
<p>The board only focuses on the strategic aspects of a file, not on the operational aspects</p> <p>47% agree 35% disagree 18% undecided</p>	<p><u>Unfavourable</u></p> <p>Some directors want to go into the details, or put differently, feel called upon to engage in the daily management...this creates some resentment in the board (R3).</p> <p>The discussions in the board are still too detailed (...) going into details may at times be good but it may not become an obstacle (R10).</p> <p>Sometimes the board gets too engaged in operational issues, too many details are being discussed (R12).</p> <p>There are being topics discussed in the board that should not come to the board in the first place because they do not have the adequate strategic level (R15).</p> <p>Too many details receive attention in board meetings, the board should only discuss major outlines (R14).</p> <p>There are always board members who want to act as managers (R8).</p>	<p>The directors trust each other</p> <p>53% agree 18% disagree 29% undecided</p>	<p>The board showed its maturity when times were difficult...there were good open discussions and the majority of the board members were trying to come to a solution as a group (R15).</p> <p>The board has done well... there are no quarrels (R9).</p>

6.5.4 Board roles and contingency factors

In the previous paragraphs, we examined to what extent structural board characteristics and process variables influence the task performance of the board of directors. In addition, our empirical evidence points to the existence of two important contingencies that appear to be critical for the board's ability to fulfil its roles.

A first category of potential contingencies that is suggested by the current findings concerns the *board's relationship with corporate management*. There is a widespread agreement that the board of directors works with and through the CEO and his management team (Conger et.al., 2001; Lorsch and MacIver, 1989). Of pivotal importance is the communication between the board of directors and management. In carrying out its duties, a board of directors needs to be well informed at all times, and information is of particular importance when a company operates in a high velocity environment (Bourgeois and Eisenhardt, 1988). Especially, non-executive and independent directors can never be as well-informed as management and they depend to a large extent on the goodwill of the latter to obtain relevant and timely information (see Chapter 5). Management is presumed to provide all relevant business and financial information for a board of directors to function effectively. Nadler (2004) noted that there are two effective ways of preventing a board from carrying out its duties, notably providing a board with too little or too much information. He referred to this phenomenon as the "dark side" of communication meaning that these practices are both effective ways of keeping a board in the dark. Of concern is that board members must be able to do more than just ask good questions. They must be sufficiently informed to challenge and contest management's view (Carter and Lorsch, 2004). In this respect, a lack of sufficient information is expected to limit a board's task performance. By means of the written questionnaire, we asked the directors to rate various dimensions of the board's information flow on a 5-point Likert type scale¹⁸. We approached the information needs of the board as they are related to the board's responsibilities. Table 34 shows the results.

¹⁸ The 5-point likert scale was labeled as follows: strongly disagree, disagree, undecided, agree, strongly agree.

Table 34: information as key aspect of board-management communication

	Evaluation of board information	Agreement*
		N=17
General	The directors are sufficiently informed to play their role and to make sound decisions	10 (59%)
	The documentation is relevant	12 (70%)
	The documentation meets the requirements and expectations	10 (59%)
Specific with respect to the board’s monitoring role	Financial information is sufficiently detailed	14 (82%)
	FIN – opinion meets the requirements	13 (76%)
	Legal - opinion meets the requirements	14 (82%)
	Information on the Company’s risk profile is sufficient	11 (64%)
Specific with respect to the board’s strategic role	Information on the strategy is sufficient	9 (53%)
	Information on possible alternatives to a resolution is sufficient	8 (47%)
	Information on the telecom market is sufficient	10 (59%)
	Information on the Company’s products is sufficient	8 (47%)
	Information on the Company’s network is sufficient	8 (47%)

* For this type of Likert scale we did not count any mean scores but rather the number of directors who either agree or strongly agree is indicated.

The quantitative findings suggest that the opinions of the Company’s directors are rather mixed. The directors appear to be quite satisfied with the information provided to the board that enables them to perform their monitoring tasks. In contrast, approximately half of the board indicated that the information falls short in helping the directors to enhance their insights into strategic issues and as such hampers the board of directors in fulfilling its strategic role. The latter is consistent with our qualitative findings. In essence, information builds trust or differently put, trust is considered to be an indicator of information flows. Interview comments point to the fact that insufficient communication between management and the board creates tensions and distrust which is perceived to be dysfunctional.

Examples R2: Especially, better communication is required between the board and management. A culture of trust is to some extent missing.

R4: I feel some distance between the board and management... the team spirit is missing, there is less confidence and latitude.. consequently someone is more rapped over the knuckles.

R9: There is a lack of communication between management and the board, board members do not know everything.

Trust in board-management relationships appears to be an important notion which has also been recognized by other scholars (e.g. Roberts et.al., 2005; Sundaramurthy and Lewis, 2003; Westphal, 1999, Aram and Cowen, 1995) and many board members identified trust as an important ingredient for board effectiveness during our first field study (see Chapter 4). Lewicki et.al. (1998) contend that trust and distrust are not opposite ends of a single continuum. The implication of this view is that it foresees the possibility of the coexistence of trust and distrust: “social structures appear most stable where there is a healthy dose of both trust and distrust -a productive tension of confidences exists (Lewicki et.al., 1998:450). In this respect, Roberts et. al (2005) argued that trust or distrust should be understood as the condition and consequence of continuous processes of accountability between the board and management. Their analysis points to the fact that trust is two-directional. Open communication by management seems to be a source of trust for outside and independent directors. Without appropriate information it is impossible for non-executive and independent board members to develop a confidence that management is focusing on the right indicators of business conduct and performance. Similarly, management perceptions of engagement and behaviour of non-executive and independent directors in support of management functioning seem to affect confidence and trust in the added-value of the board, and hence encourage (or discourage) information flows (Roberts et.al., 2005; Carter and Lorsch, 2005).

A second category of potential contingency factors that was identified by the present study concerns the *board's relationship with the company's major shareholder*. The relationship between shareholders and the board has received far less attention than the board-management link. Corporate governance experts noted that shareholders – for a variety of reasons – are not successful at communicating their preferences to boards (Montgomery and Kaufman, 2003). Although this criticism has often been uttered in an Anglo-American governance context, our findings suggest that the absence of direct links with shareholders might also affect the performance of boards in governance contexts characterized by major block holdings. In particular, an incomplete understanding of the main long term (strategic) objectives of the major shareholder(s) (and the minority shareholder(s)), as well as of their priorities, may become an obstacle for defining the focus the board has to adopt. Some comments of the Company's directors illustrate this point of view.

Examples R1: Regarding the major shareholder , it is clear that the board and management should be better informed on its strategy.... It is crucial because all strategic decisions oriented to the long term must be prepared in advance, a merger for example, one does not get into this from one day to the next.

R7: The biggest difficulty the board and management face is the obscurity regarding the major shareholder's strategy and objectives.

R8: It appears to me that there are only few (individual) contacts between the non-executives and the major shareholder, probably it would be appropriate that the latter calls them together to explain its strategic accents.

R17: A fundamental issue relates to the fact that the major shareholder does not directly reside in the board, there are no communicating vessels. A direct link is missing...

This interpretation is consistent with previous qualitative research findings on boards. The study by Hill (1995) revealed that boards felt the need to maintain good communication with their major shareholders. In particular, dialogue with shareholders related to significant developments in corporate strategy, including take-overs, has been valued.

6.6 Discussion

The objective of the case study was to examine how different determinants of board effectiveness interrelate and whether board processes have an impact on the task performance of the board of directors. A predefined research model for board effectiveness provided theoretical guidance. Clearly, an examination of a single case study should not be expected to provide definitive evidence on the adequacy of the research model. The board of directors studied shows some features which are commonly found amongst most boards of Belgian listed companies while at the same time, the board faces some specific challenges due to the Company's business environment and governance structure. As such, some particular evidence may be case-specific but at the same time evidence can be found which enables generalizability of our findings. In essence, the results of the case study suggest two important issues.

First, the field study showed that structural board characteristics are a fundamental but insufficient condition for board effectiveness. While the standard theories in board research attach exclusive attention to structural board attributes as proxies for understanding board effectiveness, our study indicates that competent people and the interaction amongst people are more critical for the effectiveness of boards. Our findings suggest that an effective board should be able to rely on a mix of competences that are in accordance with the needs of the company. In addition, an effective board should be able to forge a relationship amongst a group of strong individuals that will permit the sharing of information, the questioning and evaluation of actions while at the same time avoiding the trap of becoming too close-knit and familiar that vigilant behaviour is undermined. Furthermore, it appears that there are certain fundamental conditions that must be present in order for these dynamics to be achieved: mutual respect amongst directors and executives, openness in the exchange of information, trust and constructive debate on issues. These findings imply that a behavioural perspective is more appropriate for studying boards of directors rather than a traditional input-output model. Behavioural studies focus on actors, processes, decision-making, relationships and interactions inside and outside the boardroom (Gabrielsson and Huse, 2005). In contrast, the commonly found input-output models in board research are used to study the direct relationship between structural board characteristics and performance outcomes, assuming that the behaviour and conduct of directors can be successfully inferred from the board's demographic characteristics. Our study suggests that the relationships and interactions cannot be fully studied by using only proxies of actual board behaviour.

Second, our field study showed that the effectiveness of boards in performing their roles depends on contingencies which relate to the other actors in the corporate governance tripod. The board of directors does not operate in isolation and its latitude depends on its relationship with the shareholder and the CEO/management. The first relationship has commonly been approached in academic governance literature as a relationship of ownership and control resulting in varying views on the influence of shareholders. The prevailing view is that fragmented share ownership leads to a mass of unidentified shareholders who fail to exert much influence over boards. Dispersed shareholders are very detached from the company and mutual communication is often lacking. As a consequence, of main concern in literature is the alignment of both directors' and management's financial interest with those of the

shareholders. At the other end of the spectrum remains a system of block holdings in which major shareholders have the potential to exert strong influence over boards. In this context, much attention is paid to the problems of private benefits and rent-extractions. However, in both cases little interest and arguments are found on the value of establishing and maintaining good communication with shareholders (Montgomery and Kaufman, 2003). Our findings suggest that the lack of understanding of (major) shareholder preferences as well as the lack of clear communication lines create a barrier to the effectiveness of boards in carrying out their roles. Similar to the shareholder-board relationship, the board-management relationship has been subject to considerable debate and has traditionally also been conceptualised as a power relationship. The theoretical approaches vary substantially, ranging from the premise of control to collaboration (Sundaramurthy and Lewis, 2003). As a result, boards of directors have been pictured along a spectrum of ‘ceremonial’ to ‘operating’ reflecting a shift of power from complete CEO-domination to a strongly involved board. Our findings suggest that effective boards need to establish a working relationship with the CEO/management that is constructive and collaborative but whereby board members are not afraid to confront and challenge issues. The paradoxical combination of trust and conflict appears to be the extra ingredient required to gel competent management and competent board members into an effective board. These findings suggest the need to develop a contingency perspective in studies of boards of directors. Generally speaking, this perspective recognizes that corporate governance designs and conceptualizations are embedded in a broader institutional and social context (Aquilera and Jackson, 2003). When studying boards of directors, it can be argued that both contextual factors (such as ownership structure, industrial environment, firm life cycle) and internal and external actors (such as management, shareholders and other stakeholders) need to be taken into account.

6.7 Reconsideration of our research framework: a system view on board effectiveness

Although the findings of our study point in favour of our initial process-oriented approach, they also suggest that our model is not wholly appropriate for

understanding the effectiveness of boards. In addition, it appears that the effectiveness of boards is shaped by a complex web of interdependent variables whereby it is difficult to isolate the effects of the separate constructs stemming from theoretical assumptions. Taking these observations into account, we reconsider our initial research framework by proposing a system view on board effectiveness. In particular, we suggest that it would be more appropriate to conceptualize a board of directors as a dynamic, open social system. From this perspective, board effectiveness is approached as the result of a set of interrelated elements, whereby a change in one element will affect other elements. Besides, the more these different elements are aligned with each other, the more likely it is that the system will produce outcomes that make a board effective. Furthermore, the board of directors is considered as an open system, meaning that it interacts with its external and internal environment.

6.7.1 *Basic systems characteristics*

Considering the board of directors as a system implies that the board will display a number of basic system characteristics (Nicholson and Kiel, 2004(b); Nadler and Tushman, 1980). A first characteristic is *internal interdependence* which refers to the fact that changes in one component of the board will have repercussions for other components. For example, our study showed that the simultaneous appointment of a large number of new, independent directors (change in board composition) affects the cohesiveness amongst the board members. Second, the board has the *capacity for feedback*, meaning that the board has the potential to use information about its output to become a self-correcting system. For example, in our study the Company's board has used information about its actual task performance to (gradually) reduce the number of directors¹⁹ as well as to approve a concrete action plan for additional adjustments. The latter includes, generally reproduced, a reconsideration of the committee-policy, improvement of the communication between the board and management and the establishment of a new format for the information flow to the board. This action plan is being implemented step-wise. Third, the board, as a system, is characterised by *equilibrium* - that is a state of balance. When an event pushes the system out of balance, it will react to bring itself back into balance, although the latter

¹⁹ At the end of 2006, board size was reduced from 18 to 16 members.

could take a substantial period of time. We take the same example of the major change in the board composition in our study. This major change had led to some kind of instability in the relationships, as it takes some time for the group to adapt to the new circumstances reflecting different personalities, knowledge, skills, behaviour, information needs etc. But over time, the board will move again towards a state of equilibrium. A final system characteristic is *adaptation*. The board has the willingness to adapt to changing environmental conditions or organizational demands. For example, in our study the board of directors is faced with a rapidly changing business environment and in response it has made some changes in its composition.

6.7.2 *A congruence model for board effectiveness*

Next to its basic characteristics, a system can be described by three basic concepts, namely input, process and output, whereby the greatest emphasis is placed on the process part (Nadler and Tushman, 1980). In this respect, a system view on board effectiveness is consistent with the input-process-output approach which we applied in our initial research framework, but it enables us to add extra dimensions to the model (see Figure 14).

Input. The input in our model refers to the board's resources that are available through the board members. Board members may be described by size, composition, competence and structure. *Board size* refers to the number of board members, while *board composition* refers to the configuration of the characteristics amongst board members. Insider/outsider ratio is the usual configuration but configuration of various dimensions of diversity (such as age, tenure, gender etc.) or competences is also included. *Board competence* represents the sum of the board members' expertise, knowledge and skills. Relational or social capacity or capabilities may also be included as competence. The concepts of board capital (Hilman and Dalziel, 2003) or board intellectual capital (Nicholson and Kiel, 2004(b)) are close to our concept of board competence. Finally, *board structure* refers to the configuration of board members into board committees.

Processes. The processes in our model refer to the interactions and behaviour amongst the board members, which transform the input into output. We have

identified three board processes, namely cohesiveness, debate and conflict norms, but we recognize the fact that this list is not exhaustive. For instance, the use of power (Pettigrew and McNulty, 1998), or other dimensions of the decision-making process (Golden and Zajac, 2001) could be included.

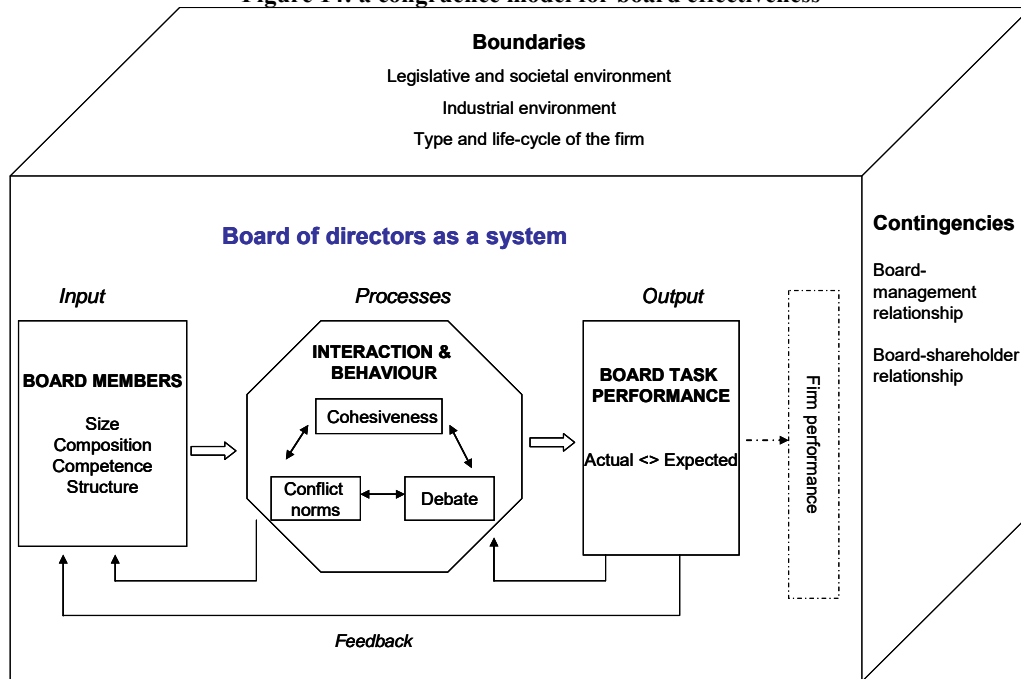
Output. The output in our model is how successful the board is in performing its dual role set.

Contingencies. Because we view the board as an open system, interacting with its internal and external environment, we introduce two contingency factors into our model. These are board-management interactions and board-shareholder interactions. As previously argued, the board of directors does not operate in a vacuum, but it interacts with other actors in the corporate governance tripod. The most important actors are the top-management team and influential shareholders, but in some cases, influential stakeholders may also be considered as important actors. Whatever the roles the board chooses to perform, it can only accomplish this by interacting effectively with the CEO/management and the influential shareholders. These interactions may take place both inside and outside the boardroom and are characterised by an apparent paradox of trust and distrust and various types and degrees of power.

Boundaries. Each board of directors has to operate within a set of 'givens', which are outside the board's direct control and which determine the boundary conditions of its effectiveness (Nicholson and Kiel, 2004(b)). We propose a set of 4 external factors that a board of directors has to face: the legislative and societal environment, the industrial environment, the type and life-cycle of the firm. The legislative and societal environment refers to the set of laws, rules and customs established by the society and which provide a board of directors with different powers or constraints. The industrial environment exposes different degrees of complexity, dynamism and technological change which impose different challenges to a board of directors. The type of the firm will determine the purpose and objectives of the firm while the major phases of a firm's development reflect past, current and future events. Both aspects are assumed to have an impact on the board of directors.

As mentioned above, we conceptualize board effectiveness as the outcome of different components that interact with each other. Of key importance is the overall alignment or ‘fit’ between the specified components (Nadler and Tushman, 1980). In other words, the congruence model for board effectiveness is based on how well its components or ‘pieces’ fit together. The basic hypothesis of this model is that the greater the total degree of congruence or fit between the various components, the more effective the board will be — effectiveness being defined as the degree to which actual board task performance is similar to expected task performance. The different components can fit well together and function effectively, or fit poorly and lead to problems, dysfunctions, or performance that is below potential. Conceptualizing boards of directors this way, implies that attention is still paid to the interconnection of structural and behavioural factors, but that we expand the initial model by introducing additional components and by emphasizing the dynamic nature of board effectiveness.

Figure 14: a congruence model for board effectiveness



6.8 Conclusion

Our initial goal was to enhance our understanding of how different factors, especially process variables, determine the effectiveness of a board of directors in performing its dual role set. Guided by a theoretical framework, we have used a single case study to examine the relationships amongst a set of predefined variables. The empirical findings highlighted the fact that our initial board model is rather incomplete. Although we have found support for structural and process variables as important determinants of board effectiveness, we were confronted with some unexpected findings. In particular, the formation of board committees, the fit between board competency and organizational needs as well as the board interaction with management and major shareholder(s) appeared to be additional factors that may hamper or facilitate the board of directors in executing its dual role set. The overall result of our study was a reconsideration of our initial board model. We have proposed a congruence model for board effectiveness whereby we conceptualized the board of directors as an open social system, made up of various components that interact with each other. It is argued that the degree of congruence between the components dictates the effectiveness of a board. Although the direct empirical evidence for this model was found at one board of directors at one period in time, it clearly points to the need for including behavioural and contingency perspectives in board research as well as for exploring multiple theoretical lenses. In understanding how board effectiveness is shaped by various interconnected components, we will be in a better position to further understand the complex relationship between the board of directors and firm performance.

6.9 References

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7 Conclusion

7.1 Introduction

The preceding chapters have outlined the importance of the board of directors as an internal governance mechanism and examined the determinants of board effectiveness both conceptually and empirically. Chapter 2 introduced the broader concept of corporate governance and described the particularities of the Belgian corporate governance environment. Chapter 2 also explained the great interest in the board of directors and discussed the different theories underpinning board research. Chapter 4 provided the analysis of the first field study which was aimed at exploring the broad spectrum of criteria, perceived to contribute to the effectiveness of boards. The findings were then used to develop a theoretical research framework in Chapter 5. The model reflects an input-process-output approach placing great emphasis on the more ‘intangible’ aspects of board effectiveness. Chapter 6 empirically challenged this process-oriented model by means of a case study of a Belgian listed company. It has documented the nature of the relationships amongst the (structural) input and (behavioural) process variables as well as their impact on the task performance of the board. The analysis has resulted in a reconsideration of the initial framework and, relying on a system perspective, a ‘congruence’ model for board effectiveness is proposed. Chapters 4, 5 and 6 represent the core of our study and unfold along a carefully chosen qualitative-oriented research methodology, explained in detail in Chapter 3.

This final chapter builds on the findings of the previous chapters to provide an overview of the main conclusions regarding the two research questions addressed in this dissertation. It also discusses the implications for science and practice. The last section outlines the limitations of the study and gives directions for further research.

7.2 Main findings and conclusions

As Forbes and Milliken (1999) note, understanding the nature of effective board functioning is amongst the most important areas of management research. Despite the fact that the board of directors is the top decision-making body in corporate life, there is relatively little known about the way boards actually operate. This stands in glaring contrast with our knowledge on what boards of directors are supposed to do. Succinctly put, the board of directors is responsible for the overall well-being of a company. Corporate governance reforms encompass various measures aimed at assuring board effectiveness in directing and monitoring a company. In addition, different forces (major corporate failures, growing directors' reliability, spread of shareholder activism etc.) and parties (institutional investors, rating agencies, media etc.) have put increased pressure on companies and their boards to fulfil their governance responsibilities. The practical relevance of studying boards of directors has triggered many scholars to investigate the relationship of boards and corporate performance. However, mainstream board researchers have remained at a considerable distance from board practice, resulting in only a shallow insight of the 'what' (the work) and 'how' (the process) of boards of directors (Leblanc and Gillies, 2005). Much of today's forces, regulations and codes are directed at improving corporate governance through the upgrading of the board's functioning. Consequently, the significant question to answer is: what determines the effectiveness of boards? For this dissertation, we have translated this question into two main research objectives: (i) *to investigate the key factors that potentially contribute to board effectiveness* and (ii) *to examine the influence of board processes on the task performance of boards of directors* (see Chapter 1). Both research questions have been approached from a theoretical as well as an empirical perspective, involving boards of directors in Belgium. We organize the discussion of our main conclusions along the two objectives of this dissertation.

7.2.1 *Insights into the key drivers of board effectiveness*

In Chapters 1, 4 and 5 it was highlighted that mainstream board research has relied on a limited number of structural board measures for studying the effectiveness of boards. Moreover, as agency theory dominates corporate governance and board research, board characteristics have been operationalised in light of the extent a board of directors is able to act independently from management. In particular, board size, the ratio of inside/outside and independent directors, as well as a separation of the positions of chairman and CEO, have commonly been used as proxies in studies to investigate the direct relationship between boards of directors and corporate financial performance. Given the great importance attached to these characteristics, we have also included them in our study. However, the findings of the empirical studies have provided a more elaborate understanding of what determines an effective board by (i) pointing out additional structural board features and (ii) directing attention to the more intangible aspects of board conduct.

The study found support for structural board characteristics...

The field study in Chapter 4 has highlighted the importance of board **composition**. It was revealed that directors value a mix of board members' roles in terms of executives, non-executives and independent directors, but its relative importance appears to be surpassed by diversity and complementarity (in skills and expertises) as well as overall competence. These latter aspects ranked systematically amongst the highest in directors' perceptions of what constitutes a good corporate board. The impact of diversity on the effectiveness of boards has been further analysed in our theoretical research framework (Chapter 5) and empirically examined in the case study (Chapter 6). Based on existing literature, it was noted in Chapter 5 that the concept of diversity embraces many dimensions and that the effects of diversity are rather equivocal as they can be both beneficial and detrimental. The case study in Chapter 6 has - to some extent - documented the importance of board diversity by pointing out the (negative) impact of directors' tenure heterogeneity on group dynamics. Furthermore, it has also reinforced the critical importance of board competence, in terms of having sufficient and adequate knowledge and skills on an aggregate level. These findings challenge the common emphasis placed on board independence as a key measure for the effectiveness of boards. In Chapter 4 it was stated that independence is the cornerstone in corporate governance debate and

research, and it is clear that the reform movement has put board independence forward as a unifying theme to improve the governance of companies (Westphal, 2002). Surprisingly, we found little evidence in our empirical studies on the independence issue. It appears that directors themselves attach less importance to - at least the structural operationalisation of - board independence. Still, they have stressed the importance of an independent state of mind. Moreover, including a sufficient number of non-executive and independent directors has been recognized as a way to broaden the knowledge base of a board of directors (Chapters 4 and 6). The conclusion that can be drawn from these findings is that *an appropriate board configuration is contended to be a first condition for board effectiveness*. Rather than approaching the composition of a board exclusively in terms of the proportion of independent directors, an appropriate board composition must be interpreted as the optimal fit between a diversified mix of knowledgeable and competent people, the roles the board wants to fulfil and the independence requirements imposed on the company.

Another structural measure put forward to enhance the effectiveness of boards are **committees**. Today's best practice governance principles as well as many listing rules demand the installation of board committees, particularly for those areas where the potential for conflicts of interest is the greatest (audit, nomination and remuneration). Especially, in the wake of many accounting scandals and unbridled CEO compensation, the requirements for audit and remuneration committees have been strengthened. In Chapter 6 it was noted that the basic rationale for the establishment of committees is a more efficient use of time, by dividing up the work amongst the directors. Board committees should allow for more in-depth discussions and the development of a specialized understanding. Although board committees have been set up by most (listed) companies in Europe and the US (see Chapter 2), academic research on their impact is scarce and mainly focused on audit committees (e.g. Spira, 2002; Daily, 1996). The findings of our empirical studies with respect to board committees are rather mixed. In the analysis of our field work, presented in Chapter 4, we could not find any indication of the importance of committees for board effectiveness. The establishment of board committees was not once mentioned as top of mind criterion for a good board of directors. Due to the lack of academic and empirical evidence, this structural aspect was not included in the initial research

framework (Chapter 5). However, the case study in Chapter 6 has shed more light on the impact of (some) board committees on the task performance of boards. In particular, it has shown that an audit committee, when certain conditions are fulfilled²⁰, is of great importance for the successful execution of a board's monitoring role. However, the relevance of a strategic committee for the performance of a board's strategic role appears to be less straightforward. The (negative) side-effects of board committees (e.g. information asymmetry, dilution of board power) are perceived to be the greatest for a strategic committee, and hence, surpass the benefits committees are supposed to yield. The conclusion that can be drawn from these findings is that *board committees are likely to enhance the effectiveness of boards but not at all costs, nor at all times*. Board committees show the full advantage for supporting a board in a successful execution of its roles only when they are (i) consciously installed and used, (ii) properly designed, and (iii) if there is sufficient and timely reporting to the full board. These are fundamental conditions for minimising the side-effects and maximising the benefits of board committees.

A final structural characteristic that has been examined is the **size** of the board. As explained in Chapter 4, board size is considered, both in academic research and corporate governance reforms, as a key determinant for board effectiveness. In fact, it is a commonly used proxy for the board's independence, together with available resources and expertise. This reasoning highlights the potential advantages of a large board. Chapter 5 has further elaborated the effects of board size and stressed the negative impact on group dynamics when boards become too large. In spite of the earlier reported mixed academic findings regarding board size (Chapter 4), the perceptions of the directors appear to be rather in favour of a limited number of board members. The results from the field study in Chapter 4 indicated that the size of the board was amongst the least frequently mentioned criteria for a good board of directors, but in the cases where it was mentioned, directors commented that a board of directors should not be too large in order to function effectively. This perception is supported by the empirical evidence from the case study in Chapter 6. The board under study was quite large, compared to the average board size in Belgium, US and

²⁰ The conditions for the well-functioning of the audit committee in this case study was its composition (independent and competent members, lead by an independent chairman), meeting frequency (min. 6 times, and shortly before the board meetings), good and timely reports to the board and the support of strongly developed internal control systems.

UK (see Chapter 2), and it turned out that this triggered various effects on the task performance of the board. Particularly, the directors stressed the negative implications of such a large board for group dynamics, and hence, indirectly for board task performance. The conclusion that can be drawn from these findings is that *a relatively smaller board size is an additional condition for board effectiveness*. Needless to say that a relatively small board size does not comprise a fixed absolute number. Rather, it should be defined as a sufficient number of directors to balance the needs, in terms of a required mix of knowledge or other resources, but with respect for the basic precepts of group dynamics and functioning.

... but suggests that intangible or behavioural factors may be the most critical determinants of board effectiveness.

In Chapters 4 and 5 it was explained that part of the inconclusive findings of research into board-performance links can be attributed to the use of incomplete (input-output) models for the study of board effectiveness. Moreover, it was noted that the common ignorance of potential intervening variables is difficult to maintain given the emergence of a new research stream that, step by step, provides a better understanding of the inner workings of boards of directors. The findings from our empirical studies have also directed attention to the importance of ‘non-structural’ board characteristics for the effectiveness of a board.

The evidence from the field work, presented in Chapter 4, suggests a prominent role for intangible or more behavioural factors as determinants of board effectiveness. A first factor relates to the **discussions** inside the boardroom. In Chapter 2, it was noted that the degree to which boards of directors engage in real discussions is still subject to considerable debate. In particular, some scholars believe that boards only act as rubber-stamping devices without real questioning or discussing of the proposals put forward by management. In contrast, it appears that directors themselves value the occurrence of debate during board meetings. During the first field study, a good board of directors was frequently perceived to be a board that exposes real, in-depth, objective discussions (Chapter 4). Chapter 5 has taken this finding into account by including debate as an intervening variable in our research framework. Moreover, based on TMT literature, it was suggested that debate, or the expression of task-

related differences, is critical for decision-making on complex tasks, as it is the case with boards of directors. This concept was also examined during the case study, and the findings supported the basic insights (Chapter 6). In particular, it appears that debate should manifest itself in a constructive way and should lead to concrete decision-making in order to enhance board effectiveness. A second factor relates to the board's **culture**. The term board culture refers to the informal rules which regulate board and directors' behaviour. As put forward by the directors, culture encompasses many aspects such as openness, exposure and tolerance of critical attitude etc.. It is perceived to be of compelling importance for the effectiveness of boards (Chapter 4). Supported by insights from the literature on group effectiveness, board culture was then conceptualised as 'conflict norms' and as such included in our theoretical framework. In Chapter 5, the role of conflict norms for board effectiveness was investigated from a theoretical point of view. It was suggested that the norms regarding conflict at force in a boardroom will dictate the extent a board engages in real discussion, and hence, is able to make optimal use of the resources provided by structural board characteristics. The case study in Chapter 6 supports this notion as the analysis pointed in favour of a board culture characterised by rather high conflict norms which permits the airing of opinions and stimulates open and candid discussions. The conclusion that can be drawn from these findings is that *structural board characteristics indicate the potential of a board of directors while its culture and its exposure to constructive discussions are the catalysts that unlock or lock this potential*. It is through board deliberations that diverse perspectives are consolidated in a critical and independent judgment of management proposals, while the culture at force is presumed to support an environment in which these deliberations can take place.

Another aspect that was brought to our attention is the impact of **cohesiveness** amongst the board members. In Chapter 5, it was documented that the concept of cohesiveness is one of the most extensively studied variables in group settings. Based on literature on group effectiveness, it was argued that the degree of cohesion plays a vital role in the communication between board members and the way they collaborate as a team. It was suggested that both ends of the cohesiveness-continuum may produce negative outcomes for board effectiveness. Succinctly put, no coherence in the board would prevent the exchange of information required for good decision-

making, while too much cohesiveness brings the danger of group thinking. The evidence provided by the empirical studies on the relevance of the concept of cohesiveness in a board context appears to be less outspoken. Issues related to the interpersonal relationships amongst board members (such as the right chemistry, trust and respect, informal contacts etc.) were spontaneously mentioned by directors as important criteria for a good board of directors, but when put at the test with other criteria, they systematically received the lowest rankings (Chapter 4). Additional comments revealed that directors view the importance of cohesiveness in the sense of the need to cherish a professional relationship amongst board members that encompasses trust and respect. It was noted that this does not imply a need for developing personal friendships or social fellowship. Also the case study has shown that directors value a minimum degree of cohesiveness in the board and that it is important to establish a sense of connectedness amongst directors, in particular when new board members are appointed (Chapter 6). The conclusion that can be drawn from these findings is that *a certain degree of cohesiveness may act as an extra condition to forge interactions amongst a well-designed mix of board members* which in turn builds trust - required for openness in information exchanges - while at the same time stimulating the occurrence of (task-related) disagreement and candid discussions.

Finally, a feature that bears special attention is **board leadership**. Chapter 4 has explained that the latter is commonly approached as a structural measure of board effectiveness. In spite of the fact that diverging theoretical perspectives exist as the extent to which the positions of CEO and chairman must be combined or separated in order for a board to be effective (Chapter 2), most corporate governance reforms have pushed for a separation of responsibilities. However, relying on insights from our field studies in Chapters 4 and 6, it appears that board leadership as a structural characteristic is of inferior importance compared to the behavioural dimension of board leadership. The role of the chairman was amongst the most cited criteria in directors' perceptions of a good board of directors and, more specifically, directors noted that the chairman actually dictates the course of board meetings. Additional findings relate to the role of the chairman in the board's decision-making process. It was indicated by the directors that for a board to be effective, a chairman should not - by all means - seek consensus. Further investigation revealed that the notion of

consensus is open to diverse interpretations and often confused with the concept of unanimity. Of essential importance in directors' perceptions is that boardroom deliberations do not depart from consensus in order to fully capture the benefits from diverse perspectives, but in the end the board should reach a decision that is supported by all the board members. Surprisingly, directors themselves did not once refer to the issue of a joint or combined leadership structure as a condition for the effectiveness of their boards. The conclusion that can be drawn from these findings is that the *leadership style of a chairman, irrespective of whether this function is performed by the CEO or not, plays an important role in the conduct of board meetings*. Its importance stems from the need to resolve apparent paradoxes inherent in the interactions amongst board members (e.g. open candid discussion while dealing with conflicting opinions, expression of dissenting views while maintaining coherence, reaching consensus after highly diverse views etc.) as well as to stimulate and preserve high standards of openness in the boardroom.

7.2.2 The influence of board processes on a board's task performance

In the discussion outlined above, the importance of intangible and more behavioural factors for the effectiveness of boards was put forward by presenting evidence of the potential impact of a board's culture, boardroom debates and board members' cohesiveness. These findings led to further investigation into how and to what extent the internal working of boards might influence the board's task performance. In Chapter 5 it was noted that mainstream board research has primarily focused on the direct relationship between board structure and board or company outcomes, and that only few studies have considered the impact of internal board processes on the effectiveness of boards. The findings of our study have shed more light on the explanatory power of board processes for a successful execution of board tasks by documenting the inevitable connection between structural board characteristics and boardroom dynamics. Moreover, they have brought to the attention two important categories of contingencies on which board effectiveness depends.

The study showed that the interaction and relationship amongst the board members impacts the way the board of directors performs its tasks...

In Chapter 5, the potential impact of a limited number of intervening process variables on the performance of a board's strategic and monitoring role has been elaborated from a theoretical point of view. A process-oriented board model was developed, drawing the indirect relationships between the board's structural input variables and the board's output. In particular, it was suggested that the emergence of debate is beneficial for the performance of board tasks because it formalises task-oriented disagreement and encourages critical evaluation of management proposals. In addition, it was noted that the effects of cohesiveness are not straightforward. Especially when members become too close-knit, it may undermine vigilant and critical behaviour, and hence, undermine a successful execution of board roles. The evidence from the case study in Chapter 6 has shown that it is difficult to isolate the effects of the separate variables (pictured in the theoretical research framework), as the effectiveness of a board is shaped by a complex web of interdependent factors. In essence, the findings have pointed out that the board of directors is not an entity that functions independently of its members. It is a group of people urged to work together to fulfil board functions in a collective manner. The extent to which the board is successful in executing its expected roles, depends not solely on the individual competences of board members (chapter 4 and 6) but also on how these competences are leveraged by the way the individual directors interact inside and outside the boardroom. Chapter 6 has noted that an unequal level of directors' competence (in terms of experiences and insights into the business) influences the nature of boardroom deliberations and, subsequently the degree to which the board is able to fulfil its roles. It was also highlighted that informal contacts are perceived to further coherence or the "team spirit" amongst board members. This permits the sharing of information and as such contributes to board task performance. Cohesiveness and debate are two expressions of how individual board members interact (behaviourally and verbally), within the context of the board of directors, aimed at collectively performing the strategic and monitoring tasks. The conclusion that can be drawn from these findings is that, rather than treating the board of directors as an abstract body, *the board of directors should be approached as a social unit, in which the combined action of individual member features and interactions amongst the members, define its internal working and, in the final end, the effectiveness of the board in performing*

its tasks. As in many things, the effectiveness of a board of directors depends on the collective performance of its members.

...but also found that a successful execution of board tasks depends on a board's relationship with management and with its (main) shareholders.

In essence, corporate governance is about the division of power and organising accountability between the three actors in the corporate governance tripod: the shareholders, management and the board of directors (Chapter 2). As demonstrated by the case study in Chapter 6, the board of directors does not operate in a vacuum, and for a successful performance of its tasks, the board can not be isolated from management and the shareholder(s). The relationships between these three anchors have been subject to considerable debate and are commonly conceptualised as power-relationships (Chapter 2). First, the board-management relationship has often been approached in black and white terms, namely as a relationship of boss versus subordinate. Driven by various forces²¹, the widespread view is that CEO/management can not be trusted because they may not act in the shareholders' best interests, even engaging in potentially damaging behaviour. Boards of directors, in particular independent directors, are presumed to act as 'policemen' to keep management in control. The evidence presented in Chapter 6 has shown that the relationship between the board of directors and management is much more complex. In particular, it appears that both collaboration and control are key to developing an effective working relationship between the board and management. A determining issue in this relationship is the communication between the two parties involved. Chapter 4 has already pointed to the importance of the information flow for the effectiveness of boards. Directors perceived the information that is provided before the board meetings as vital for a board to function well. The evidence from the case study has reinforced these findings (Chapter 6). It was noted that timely and sufficient information, that serves both the board's monitoring and strategic role, as well as openness in communication are essential for a successful performance of board tasks. Moreover, an additional issue that was brought to our attention is the importance of

²¹ Forces include, among others, the popularity of agency theory, a research tradition based on US-practices and embedded in a US-governance context; not to mention the impact of the recent wave of corporate malpractices.

trust in board-management relationships. In the first field study, trust between the board and the CEO/management was ranked high amongst the most important ingredients for an effective board of directors (Chapter 4). The case study in Chapter 6 has shed more light on the impact of trust. It was pointed out that trust is an important indicator for the information flow. Building trust, and subsequently, enhancing openness in information exchanges, implies the same (behavioural) standards for both directors and management. More specifically, outside independent directors should not seek to assume an executive role while management should not seek to minimize the role of the non-executives by hiding or withholding information. The conclusion that can be drawn from these findings is that, instead of approaching board-management relationships in hierarchical terms, *the board of directors and management should develop a partner relationship that is characterised by open exchanges of information, a coexistence of trust and critical monitoring as well as a clarity about the role of the board vis-à-vis the CEO*. Even when the board has the appropriate structure and processes in place, it is contended that a lack of information will hamper the board of directors in executing its roles successfully. Moreover, trust and latitude are equally important in the board-management relationship as well as a mutual understanding of each others roles and responsibilities.

Second, the board-shareholder relationship has also been subject to considerable debate. Succinctly put, dispersed shareholdership, leading to a multitude of non-influential shareholders versus concentrated ownership, leading to strong, powerful majority shareholders, are the opposite ends on a single continuum. In both cases, the power bias is the source of different governance “diseases” such as management entrenchment (dispersed shareholdership) and extraction of private benefits (concentrated shareholdership). Consequently, a major part of the corporate governance debate and the governance reforms concern the design of required checks and balances (Chapter 2). However, in Chapter 6 we have noted that the value of establishing and maintaining good communication with shareholders is an issue that has received far less scrutiny. This phenomenon has been referred to as the ‘missing link’ in the corporate governance triangle, indicating that strong accountability between shareholders and the board of directors is often lacking (Montgomery and Kaufman, 2003). Our study, conducted in a corporate governance environment, characterised by concentrated ownership patterns and long-term committed

shareholders, challenges this notion. In such a context, shareholders with an important stake (will) commonly sit in the boardroom (Chapter 2), and by definition, maintain close and active connections with the board of directors. In contrast, the relationships of the board with minority shareholders or large shareholders who are not directly present in the boardroom are more complicated. In many instances, there is fewer or no direct contact between these shareholders and directors (who serve on their behalf). For these shareholders it is more difficult to articulate their goals and make their preferences known to the board, while for the latter it is more difficult to understand what shareholders want. During the first field study, directors commented that a good board of directors is able to translate the main shareholder's strategic ambitions to management. The evidence of our case study has also highlighted the importance of clear communication between the board and its major shareholder as well as a good understanding of the major shareholder's (strategic) preferences for a successful execution of the board's strategic role (Chapter 6). The conclusion that can be drawn from these findings is that *the board of directors must develop proper communication lines with shareholders, in particular with the most influential shareholder(s), while preserving the required independence to prevent abuses by the influential shareholder(s)*. It is contended that shareholders, both majority and minority shareholders, also breathe expectations regarding the performance of board roles. Bringing actual performance in line with these expectations requires an informed board. For major shareholders, who are on the board, the exchange of information of their objectives is quite straightforward. For those shareholders who are not on the board, the board of directors should enter into communicative relationships to assure clear understanding of mutual objectives and concerns. In addition, it is important that the major shareholder(s) look with an impartial eye towards improving the company's future. Only then can directors be effective fiduciaries and good bridges to other (minority) shareholders. After all, the role of the board of directors is to safeguard the interest of all shareholders.

7.3 Implications of the study

Supported by the main findings and conclusions outlined above, our research has important implications for science and practice. First, we discuss the implications for

management science. Second, we provide an overview of the implications for practitioners, such as companies, institutional investors, other market parties or policy makers.

7.3.1 Implications for management science

This research makes a number of contributions to management science. A first contribution stems from the study of boards of directors **in a non-US context** using an **alternative research methodology**. In spite of the intense research interest in corporate governance systems and mechanisms around the world (Schleifer and Vishny, 1997), most (empirical) studies on boards of directors have been carried out using samples of large US corporations and are inspired by quantitative US research traditions (Huse, 2005). The latter implies that scholars have mainly applied board data, retrieved from publicly available resources, or - to a lesser extent - questionnaire data obtained from management. This approach has contributed to the knowledge on boards of directors but scholars have acknowledged that alternative research methods are necessary to make considerable progress in board research. Zahra and Pearce (1989) stated: “Thus far, secondary references and surveys, completed by management, have dominated the literature. We recognize the importance and richness of these data sources, but we urge researchers to consider incorporating directors’ views in the study of board behaviours, supplemented by the researchers’ secondary data with their observations of board attributes.” (p.330) Although their call dates from almost two decades ago, qualitative studies on boards of directors as well as research of boards in European contexts are still very scarce. The lack of these studies is caused by the fact that (i) access to boardrooms and directors remains difficult both in the US and in Europe; and (ii) the European governance environment does not constitute a homogeneous unit. Compared to the US, Europe embraces a greater diversity in terms of ownership patterns, organization of boards (1-tier and 2-tier), size and use of stock markets etc. (Van den Berghe et.al., 2002). The larger variation amongst European countries may hamper board research, as scholars are faced with relative small samples (per country) and enhanced complexity when controlling for context in cross-sectional or cross-country studies. In our study, we were able to examine the determinants of board effectiveness through a direct contact

with boards and directors in one country. As such, our research contributes to reduce the identified gap in existing board literature by studying boards of directors in a Belgian context using a qualitative-oriented research approach (mixed methods and case study design).

Second, our research contributes to corporate governance and board literature by documenting an **indirect route**, including **novel research areas**, for investigating board-performance links. Mainstream board research has tended to overemphasize the direct link between board characteristics and financial firm performance (Daily et.al., 2003). The latter has been used as a proxy for empirical testing of a board's effectiveness in protecting shareholders' interest (Coles et.al., 2001). In addition, most scholars have focused on a limited number of structural board measures for investigating the impact of boards on the performance of firms. Years of research into these direct causal relationships have resulted in conflicting results, raising doubt on the explanatory power of these input-output models for the study of boards. In addition, although scholars recognize that the human dynamics of boards are as important (if not more) as the structural composition of boards in determining their effectiveness (e.g. Sonnenfeld, 2004), these aspects have rarely been included in empirical analyses. A common feature of this stream of research is the treatment of the board of directors as a "black box". This resulting gap in knowledge has triggered the awareness to look for indirect board-performance links, to explore intervening variables as well as to better understand how boards of directors actually function. Our research has omitted a direct link between the board of directors and corporate financial performance by proposing an input-process-output model for board effectiveness. Our model is not unique in its nature, as other notable scholars have provided similar (indirect) modelling of board effectiveness (Huse, 2005; Nicholson and Kiel, 2004; Forbes and Milliken, 1999; Zahra and Pearce, 1989). Still, our research contributes to literature as it strongly relies on extensive field work for the development as well as the validation of the model. In particular, an exploratory field study has been used to evaluate the usefulness of existing models in literature and to carefully select relevant constructs (which go beyond the 'usual suspects' (Finkelstein and Mooney, 2003) of board effectiveness) in order to build an own theoretical research framework. Next, we have subjected our framework to an empirical

challenge by means of a case study. This has generated a refined model that is substantiated by contemporary field study of board effectiveness.

A third contribution provided by our research is the response to calls for board studies using a **pluralistic theoretical lens** (Daily et.al., 2003; Lynall et.al., 2003; Hilman and Dalziel, 2003, Johnson et.al., 1996; Judge and Zeithaml, 1992). There is no doubt that agency theory dominates corporate governance and board research. Agency theory is concerned with resolving conflicts between the agent (management) and the principal (shareholder). It owes its popularity to the fact that it is a relatively simple theory, relying on an old, widespread (economic) notion (self-interested behaviour of humans) (Daily et.al., 2003). As such, conceptualisation and empirical studies of board effectiveness have mainly been concentrated on how to protect shareholders from (potential) managerial abuses of corporate resources. A board's monitoring role and the empowerment of the board, by increasing its independence from the CEO, have received the most research interest. Although other theories are recognized in corporate governance research, their use in empirical studies remains inferior to the agency perspective. Moreover, theoretical foundation in board research is to a large extent fragmented as most studies apply only one single perspective. However, it appears that this approach has provided academics with insufficient insights into actual board functioning (Daily et.al., 2003). In fact, board effectiveness is such a complex phenomenon, that not one theoretical perspective can fully capture all dimensions. Our research has embraced various theoretical perspectives both in conceptualising board effectiveness as well as in explaining empirical findings. Some examples: the study combined agency and stewardship theory to define the board's dual role set (monitoring and strategic function); insights from resource dependency theory are relied upon to discuss the notion of board diversity; system theory is introduced to develop a 'congruence' model for board effectiveness etc. The co-existence of multiple theories has allowed for a more complete board model and a richer understanding of how boards can be (un)successful in the execution of their roles.

Finally, our research contributes to **other research streams**, in particular the literature on organizational demography. An impressive amount of field research exists on how group demography impacts group processes and performance. It has

been well-documented that the demographic composition of groups can influence their effectiveness both directly and indirectly (Williams and O'Reilly, 1998). Especially, more recent studies have been quite successful in bringing the explanatory power of intervening process variables to researchers' attention. However, when studying the 'group' phenomenon within an organization, scholars have traditionally focused on work groups and top management teams (TMT). The empirical definition of TMTs varies considerably and in some cases, executives who serve on the board of directors are included (Carpenter et.al., 2004). So far, the literature on group and TMT effectiveness has directed little research attention to the study of boards of directors. Similarly, mainstream board research has no tradition of considering a board of directors as a group or team. One reason may be that boards of directors expose some specific features which distinguish them from other organizational groups (Forbes and Milliken, 1999). Still, there is a growing belief that effective boards are those who are able to function as high-performing teams (e.g. Nadler et.al., 2006; Charan, 2005; Carter and Lorsch, 2004). Our research approaches the board of directors as a team and examines the relevance of a limited number of constructs, frequently found in group and TMT studies, in a board context. Furthermore, our research also used concepts from social categorization and similar/attraction theories to predict the effects of diversity when applied to boards. As such, our research is an attempt to bridge the gap between two research streams and traditions.

7.3.2 Implications for practitioners

7.3.2.1 Companies

Two general observations are of concern when discussing corporate governance at a company level. It is clear that corporate governance is not an end in itself, but a means to achieve the corporate objectives and strategy. Corporate governance needs to put in place the structures and processes which make it possible for a company to pursue its strategy and hence improve its performance. One of the most important governance devices, in this respect, is a company's board of directors. Boards of directors are assumed to create value by enabling management to make better decisions and to run

the company more effectively than would be the case if management would act on its own. At the same time, companies are facing the pressure for good governance from the shareholder community and from the public at large. Increasingly, various market parties are demanding companies to implement rigorous corporate governance principles in order to achieve better returns on their investments. The often cited McKinsey studies have shown that an overwhelming majority of investors are prepared to pay a premium for companies with high governance standards. In this respect, installing the proper corporate governance mechanisms provides the company with a competitive advantage in attracting capital, reducing the financial risks for investors, and consequently, the cost of capital (Van den Berghe and Levrau, 2003). In response to both observations, we believe that the contribution of our study for companies is two-fold.

First, the study provides a better understanding of what factors may contribute or hamper the board in performing its dual role set (monitoring and stewardship). As such, the findings could serve the purpose of **board evaluations**. Board evaluations are considered to be one of the most promising tools for enhancing board effectiveness, and subsequently, stimulating good corporate governance practices. Not surprisingly, board evaluation is a common recommendation in many, if not all, corporate governance codes. The purpose for boards is to assess their own performance in order to get feedback on how well they are doing. A well-conducted board evaluation should give a clear picture of the strengths as well as the opportunities for change and improvement. Moreover, a formal board evaluation signals to the external world that the company is willing to comply and live-up to the highest standards of governance. However, in practice, companies are still struggling with questions on how to conduct a(n) (self-)assessment that goes beyond a mechanical process of checking off items on a list that ultimately has little real value for the board. Our study has identified different variables and relationships which appear to be of critical importance for the effectiveness of boards. As such, it provides a first answer to the question as to what kind of issues to address in value-adding board evaluations.

Second, our findings with respect to board composition (input) and board inner working (process) may have practical relevance for the **selection of (new) non-**

executive, independent directors. For years, the recruitment of these directors has taken place in an informal way, which stands in glaring contrast to the professional selection procedure of top management. In many cases, the boardroom has been populated with directors attracted from the ‘old boys network’ without paying much attention to directors’ qualifications. In the wake of the many corporate governance reforms, this practice is changing due to the growing request for independent directors. When searching for non-executive independent directors a more careful screening of the qualities required - with respect to the question of independence - is happening. In contrast, the use of a formal selection profile, taking into account the required competencies that directors must have to be effective on a board, is not yet common practice. Our study has pointed to the importance of having an appropriate mix of competences on board in line with the roles the board is expected to fulfil as well as in line with the needs of the company. Our findings substantiate the often heard call of other scholars to develop a competence matrix when selecting new board members (e.g. Leblanc and Gillies, 2005; Cascio, 2004). These matrices are practical instruments for matching directors’ characteristics with the key areas of expertise needed, currently as well as in the future, in order for the board to function effectively. Still, a company must be aware that the validity of such matrices is not perfect as they do not measure the behaviour and interpersonal skills of directors. The will to engage in constructive debate, to embrace or challenge the existing norms and to develop the ‘chemistry’, are not guaranteed by expertise and knowledge. Our study has shown that the ability of directors (‘can-do’) and the behaviour (‘will-do’) are both critical factors for a board to be effective. As such, both aspects should deserve equal attention in the selection process, although we acknowledge the fact that the latter is more difficult to assess accurately.

7.3.2.2 Institutional investors and other market parties

For decades, institutional investors have been prominent actors in fostering and enforcing good governance. They believe that the governance of a company affects the financial risks of their portfolio. Issues of corporate governance are put on a par with financial indicators, when evaluating investment decisions. Furthermore, institutional investors pay much attention to the board of directors for safeguarding

their interests. The growing interest of institutional investors in the corporate governance practices of companies has stimulated the emergence of governance and board ratings. For some years, the scoring of corporate governance has been used in most capital markets. Rating systems are increasingly considered to be strategic instruments not only for potential investors but also for creditors and even for the public at large (Van den Berghe and Levrau, 2003). However, institutional investors and rating agencies operate at a distance from the boardroom, making it nearly impossible to evaluate the way the board of directors performs its roles. They draw confidence from board features that are visible from the outside (for example, the number of independent directors) and treat them as prerequisites for an effective board.

Our study sheds more light on the key determinants of board effectiveness and has highlighted the danger of limiting attention to structural board measures. We found that the effectiveness of a board is shaped by a complex web of variables that encompasses both structural and behavioural aspects. Moreover, the study has shown that board effectiveness depends on the interaction with other actors in the corporate governance tripod. We believe that these findings have three important implications for the external evaluation of board effectiveness, as done by institutional investors and rating agencies.

First, the evidence of our study stresses the need to refine **the scoring criteria** used by investors and rating agencies to assess the quality of a company's board of directors. Any system of assessing board effectiveness implies a tension between objectivity and subjectivity, and faces a trade-off between (easy to address) 'hard' and (difficult to address) 'soft' factors. Unfortunately, in many cases, market parties follow a "box ticking approach" to measure boards of directors, an approach which we consider scarcely advisable and even unfair (Van den Berghe and Levrau, 2003). Including the more intangible side of board practice implies a broader and different evaluation approach as well as closer and more frequent contact with the company and its board members.

Second, our study provides some scientific foundation for **the weighting methodology** underlying external evaluations. Most institutional investors and rating

agencies assign weights to the evaluation indicators. Different weights are given to detailed criteria and/or global categories in the scoring devices depending on their priority (Van den Berghe and Levrau, 2003). Until now, these priorities have been determined by discrete parties, especially investors, without strong academic backing regarding the explanatory value of the criteria and their assigned weight. For example, when assessing board composition, much attention is paid to the appropriate mix in terms of inside, outside, independent directors. Our findings have highlighted the importance of diversity and complementarity in directors' expertise and knowledge, and suggest a reconsideration of the relatively high weight assigned to board independence.

Third, the study also suggests building in sufficient **flexibility** when assessing the quality of boards of directors on a global scale. Critique has already been uttered on the use of a 'one size fits all' approach in assessing corporate governance and board practices of individual companies. Our study of boards of directors in a Belgian context has pointed to the impact of the governance environment and the ownership structure on the organisation and functioning of boards. More specific, our findings have indicated that the effectiveness of a board results from a fit between many components, and that the 'ideal' configuration will vary according to important contingencies while also depending on a set of boundary conditions. Many of the most influential institutional shareholders and rating agencies have Anglo-American roots and base their evaluations on 'best practices' from an Anglo-American governance context. Moreover, their investment strategies are commonly aimed at large public companies, whose size exceeds that of many European listed companies. Assessing the effectiveness of boards with the same standards, conceptions and measures in all circumstances appears to be inappropriate and may create a false sense of confidence. The real challenge for rating agencies is to find the right balance between the degree of globalisation in their scoring (to compare companies on a worldwide base) and the degree of differentiation (to take into account national and company differences).

7.3.2.3 Policy makers

Corporate governance issues are of international interest and have influenced the public policy dialogue globally. Of common interest is the stimulation of a governance environment for (economic) wealth creation and to safeguard the competitiveness of businesses and financial markets. As many corporate failures have shocked the world, the regulatory context has changed rapidly in order to address corporate governance-related risks and abuses, hoping to rebuild trust. It must be noted that the reaction of policy makers in the US and Europe evolved differently. While the US opted for a more prescriptive and legalistic approach to governance regulation, Europe reacted with a more flexible ‘comply or explain’ approach, perceived as offering a ‘lighter’ regulatory environment (Dallas, 2006). It is not our ambition to launch a discussion about the most effective regulatory framework. In contrast, it is striking to see that notwithstanding the different approach, the governance reforms in the US and in Europe breathe similar calls for further strengthening board independence and the control function of board of directors. Both ‘hard’ and ‘soft’ law (e.g. corporate governance codes) are seeking to enhance the effectiveness of boards and place great emphasis on changes in visible, structural characteristics in order to (re)install confidence. In this respect, there appears to be no difference with the behaviour of investors and rating agencies (see discussion in paragraph 7.3.2.2). Our study is a modest attempt to provide some academic evidence for current and future governance reforms from two perspectives.

First, our research has begun to identify some of the key issues that promote effective boards. The key issues span individual and group levels, as well as structural and behavioural levels. As mentioned before, most of these issues are difficult to grasp from the outside and even harder to regulate, apart from the question whether there is a need to regulate these issues at all. We believe that ‘soft law’ is a valuable instrument but our study suggests to policy makers and other bodies involved, to embrace **a broad and flexible perspective in designing, adapting and monitoring corporate governance codes**. A broad perspective refers to the fact that policy makers should strive for (national) recommendations which can stand the test with international standards while at the same time promoting more ‘intangible’ aspects of board and governance practices. A flexible perspective refers to the fact that policy makers should go beyond the international tendency of focusing almost exclusively on the monitoring role and on empowering the control capabilities of a board. As our

study also highlighted the role of the board of directors in the strategic process, more attention should be paid to directing reform efforts at stimulating or enhancing a board's strategic capabilities. The Belgian Corporate Governance Code, for example, already reflects this broad and flexible approach. It provides rigorous prescriptions regarding structural aspects, like board independence; but it also includes a relatively broad range of guidelines regarding leadership of the board, board room culture, individual director's behaviour and board interaction with management as well as with shareholders. Furthermore the Code departs from the assumption that striving for a proper balance between entrepreneurship and control as well as between conformance and performance is key in developing an appropriate governance model.

Second, policy makers should reflect about ways to **balance the benefits and costs** of governance reforms. They can do so by focusing their efforts on measures that enhance actual board effectiveness and that - at the same time - are perceived to enhance effectiveness by those parties operating at a distance from boards. A concrete example can be found in the wave of (legal) propositions to increase the ratio of women on boards of directors. From a corporate governance point of view, this evolution looks promising because it is aimed at (i) broadening the pool of directors, opening the 'old-boys' network by forcing companies to look for female candidates, (ii) bringing in new, different insights to board room discussions as it is common knowledge that men and women approach things differently, and (iii) seeking a 'balanced' board composition in terms of a more fair representation of society. However, the danger in the plea for greater gender diversity is that it may serve political rather than governance purposes, while at the same time imposing additional costs for many companies to live up to these requirements, without really contributing to the effectiveness of their boards. Our study has pointed out that gender is only one (minor) dimension of board diversity and that attention should be paid to a mix of adequate competencies when composing a board of directors. In this respect, we suggest that policy makers change the narrow focus and incorporate the issue of gender representation into the broader debate of enhancing board diversity. Furthermore, given the emphasis our study places on board competence, policy makers could stimulate companies and individual directors to take training courses in order to enhance or refresh specific knowledge. Governments could do so by introducing tax-friendly mechanisms, such as the 'education cheques' previously

issued by the Flemish government in Belgium. Board diversity and competence are characteristics presumed to contribute to the effectiveness of boards and, combined with sufficient transparency on a director's track record (for instance in the annual reports), are possible to evaluate from the outside.

7.4 Limitations of the study

The interest to study the determinants of board effectiveness encompasses an ambition to come as close as possible to the actors involved in the work of boards of directors. The conceptualization and understanding of how the effectiveness of boards is shaped by a complex web of interdependent variables also requires a close access to the directors' interpretations of their actions and interactions with others. This puts challenging demands on researchers when it comes to selecting and using appropriate methods to gather empirical material as well as to balancing the necessary ethical considerations. Our study was carefully designed in order to establish consistency with the existing knowledge in the field, the research questions and the methods used (Huff, 1999). Still, it is stated that it is not possible to do an unflawed study (Scandura and Williams, 2000). As usual, specific choices had to be made to carry out the study and any choice has inherent flaws. Our study faces some limitations, related to both the research methodology and the scope, which need to be recognized.

7.4.1 Methodological limitations

Our study is characterised by a coordinated qualitative research methodology and as such strongly relies on qualitative data. This type of study is still rare in board research, even if there are some exceptions (e.g. Huse et.al., 2005; Leblanc and Gillies, 2005). Notable reasons for the lack of such qualitative studies are difficulties to obtain access to directors or boardrooms and the large workload they often demand. Thus, being able to conduct such a research can be considered to be a contribution in itself (Daily et.al., 2003). However, the **use of qualitative data** is quite challenging because it is often criticized to be less objective compared to quantitative data. The qualitative data, included in our study, was entirely **retrieved from field interviews**.

Interviewing is one of the most acknowledged and useful ways of investigating how actors experience and interpret their everyday life (Fontana and Frey, 2005; Stake, 2005), and is presumed to be critically important for helping to understand complex organizational phenomena, such as boards of directors (Judge and Zeithalm, 1992). At the same time, this implies that the topic under study (board effectiveness) is based on the *perceptions* of the selected respondents. Research into director's own perceptions of their role(s) is suggested as a future avenue in board research, rather than searching for 'objective' measures of effective boards (Johnson et.al., 1996). However, as with all interview-based research, there is no sound argument to assure that perceptions accurately reflect reality (Hill, 1995). In addition, it is well-known that research based on self-reporting may suffer from a phenomenon known as *social desirability*. The latter refers to the inclination either to present oneself or an issue in a manner that will be viewed favourably by others and/or to preserve a self-esteem (De Pelsmacker and Van Kenhove, 2005). Especially, when sensitive issues are being surveyed (e.g. the relationships amongst the board members), there exists a risk that answers are biased and confound results. The social desirability bias may be enforced by the lack of random selection of the respondents in our study. There exists the possibility that those who participated in the study did so due to their interest in corporate governance. As a consequence, the respondents may have not provided an entirely accurate or unbiased characterization of board effectiveness and its determinants. The threats of subjectivity and social desirability are both inherent to field studies and can not be fully avoided. However, it is important to pay attention to these aspects and to limit the potential bias as much as possible. A commonly accepted manner to tackle the risks and problems associated with qualitative field research, is the technique of *triangulation* (Jick, 1979). Triangulation can be applied to many elements of research methods, including strategies, settings for data collection, and sources of data (Scandura and Williams, 2000). To increase the (internal and external) validity of our study and the reliability of our findings we place great emphasis on triangulation in all of these three dimensions. On the global level, we have combined two different research strategies (mixed methods research design and case study design) for conducting the field studies. On the sub-level, we have used multiple sources of data (qualitative and quantitative) and multiple investigators were brought in for collecting the data during the interviews. Thus, in both (empirical) parts of our study, we

combined a variety of evidence either to elaborate (as part of the mixed methods research design) or to corroborate (as part of the case study design) the findings.

A second methodological limitation is related to the **choice of a case study** as the research strategy for the second part of our study, which is the validation of our board effectiveness model. One of the most heard critiques on case study research is the lack of *generalisation*. The latter refers to the extent to which the results and conclusions can be transferred beyond the particular context in which they were generated (Yin, 2003; Eisenhardt, 1989). Applied to our research, some factors must be considered in relation to the study of a single board of directors. Although our focus is justified and has shown important benefits, caution is required when generalising the case study results to other boards of directors. It is important to remember that boards of directors do not constitute a homogeneous population. There are several features and circumstances that make boards similar but at the same time, there are also many features and circumstances that cause differences between board of directors. The proposed relationships were studied for a board of directors facing many challenges related to the Company's governance structure and its business environment. Strictly speaking, our case study findings are only generalisable to other boards with similar characteristics and who are confronted with similar challenges. There are reasons, however, that our case study may have broader applicability to research on other boards of directors. In particular, Yin (2003) clarifies the problem of generalisation by distinguishing between statistical and analytic generalisation. The former, which is common for survey research, requires a representative sample of the population. By means of statistical frequencies and tests, generalisation to the population is obtained. The latter, which is typically found in case study research, does not require a (statistical) representative sample because this kind of generalisation is aimed at expanding and generalising theory. Having said this, our empirical and theoretical interpretations put forward by the case study can not be generalised to a wider population of boards of directors in a statistical sense. Rather than generalising to a population of boards, the aim has been to generalise to theory and to create conceptual and theoretical notions that are potentially applicable and transferable to other contexts. During the case study, analytical generalisations through the use of existing theory and earlier relevant studies have been made systematically and step by step in a transparent way. In particular, we have compared our findings, based on the search for

patterns and relationships, with our research framework as well as with literature discussing similar findings in various contexts. This allowed us to reconsider our initial board model by refining the assumptions and the proposed relationship amongst the variables. As such, our theoretical model can be used as a point of departure for other researchers who wish to examine the issue of board effectiveness, in other types of firms or in other environmental contexts. We acknowledge the fact that the differences amongst firms and environments reinforce the importance of examining variation in the effectiveness of boards across a variety of populations, while larger samples are needed to test the robustness of our results and our model. In this respect, the applicability and transferability of the results to wider populations in a more statistical sense, remains a question for further research using other research methods and analytical techniques.

7.4.2 Scope limitations

The scope of our study is limited by at least four decisions. First, we have focused our study on **the determinants of board effectiveness**. We have looked into the ‘drivers’ of board effectiveness, how they interact and how they may influence the board in performing its roles. We have not investigated any kind of relationship with firm performance, as has been the case in many other studies on board of directors. As such, we are unable to conclude upon the way the effectiveness of boards influence firm performance.

Second, we have limited the field study to **boards of directors of Belgian companies**. Focusing on boards of directors in a non-Anglo-American context has the potential to provide additional insights on the effectiveness of boards in other governance environments. In addition, it helps to evaluate the applicability, in other research settings, of commonly used board concepts and theories which originate from the corporate governance discussion and research in the US. At the same time, particularities of the Belgian governance environment as well as the cultural setting, may influence the way board members perceive the effectiveness of their boards. Hence, caution is required when comparing empirical findings from studies that are conducted in different contexts.

A third scope limitation relates to **the time-frame** of the study. The empirical study in both parts of our research, is conducted at one moment in time. Our findings prove valuable insights into the concept of board effectiveness and its determinants, but we still give a one shot picture. As any organizational phenomenon, boards of directors are not a static given nor do they operate in static circumstances. The evolving character of environments and organizations as well as increased public pressure on boards of directors makes any findings on the effectiveness of boards very temporary.

A final limitation of the research is our limited ability to grasp the **complexity** associated with opening the “black box” of actual board functioning. Therefore, we had to build in limitations to the number of variables that could be studied. For example, we have only focused on three intervening process variables for a better understanding of how group dynamics impact the execution of board roles. Although the board of directors is considered to be a decision-making group, we did not investigate the process nor the style of the decision-making. The characteristics related to decision-making may also influence the effectiveness of boards in performing their roles and as such, provide valuable variables to be additionally included in board research.

7.5 Directions for future research

Research often raises more questions than it answers. A positive aspect of the limitations described in the previous section, is that they generate ideas for future research. We will address a number of avenues for future research that we consider especially worthwhile to explore.

A first step in future research on the topic of board effectiveness should be **the validation of our theoretical model on a larger scale**. The main purpose of the study was to identify, by means of extensive field studies, the key determinants of effective boards and to examine how they interact. The rationale for the study stems from a belief that traditional proxies do not fully capture actual board conduct resulting in incomplete input-output models. We have found support to include

additional proxy variables for the study of board effectiveness and put them together in a more comprehensive research model. In this respect, it is advocated to validate the new proxies and the research framework that are suggested by this study. The suggestion for further research in this area unfolds along three lines. First, a similar qualitative-oriented research can be useful to validate the research model for *different types of firms, for different stages in their life cycle and for different (financial) circumstances*. The central postulate of the research model is an overall fit between the various components. It can be stated that a specific configuration of board attributes that are beneficial for one company, for one period in its life cycle or for one kind of circumstance may turn out to be detrimental for another. Family firms, high-tech, venture-backed companies and non-profit organisations are some examples of companies which expose different governance structures and processes (Van den Berghe and Levrau, 2002; Forbes and Milliken, 1999). Hence, the application of the notion of board effectiveness may vary according to the type of firm. Similarly, the stage of a firm's life cycle (e.g. entrepreneurial versus maturity) (Lynall et.al., 2003) as well as its situation in times of crisis versus going concern (Daily et.al., 2003) are different circumstances that may impact the particular congruence between board inputs, processes and output. Including different firm types, from various life cycle stages, operating under different (financial) circumstances would shed more light on the conditions under which a board of directors can or will be effective in performing its roles. Second, we suggest the use of *other research strategies* that are more suitable for sample generalisation. In particular quantitative research methods, such as survey research, can cope with large samples and allows the making of statements for a larger population. Quantitative research techniques are designed to test the identified relationship amongst the variables on a large scale and are thus well-suited to check the robustness of our proposed proxy variables as well as test the model, in general. Third, we suggest expanding *the research sample* of Belgian boards of directors to include an international scope of different countries. At first glance, it would be interesting to apply our research model to Anglo-American boards of directors as they have traditionally been the focus of mainstream corporate governance research. In addition, it is worthwhile to investigate boards of directors in other European countries. Within Europe, the corporate governance environment differs substantially and boards of directors in some countries are organised in a different way (two-tier

board structure versus one-tier board structure). An enlarged sample would further improve the quality and the robustness of the proxy variables and the research model.

A second step in future research is the need **to link board effectiveness with financial performance**. A large amount of empirical literature on boards of directors examines how board characteristics relate to profitability. We have referred to the difficulty to study this kind of direct relationship between board inputs and company performance. It was noticed that firm performance is a complex issue, hard to measure and that it is finally the outcome of many inter-locking factors. For this reason, we have focused on the study of board effectiveness assuming an indirect link between board inputs and corporate performance outcomes. Nevertheless, more insight into the relationship between board effectiveness and a company's financial performance would be useful. In this study, board effectiveness has been approached as the successful execution of a dual role set. Although, we advocate a certain balance between the board strategic and monitoring tasks, it is acknowledged that the predominance of one role over the other may vary amongst companies. In this respect, we suggest to further investigate the implications of the predominance of either the strategic or monitoring role on the financial performance of a company. For example, it can be investigated whether companies show better performance outcomes, in terms of higher growth rates when their boards put great emphasis on their strategic function. It is equally interesting to investigate whether a strong emphasis on the board's monitoring and control tasks will result in a more stable performance but at lower levels of growth. Practitioners and (institutional) investors are especially interested in the impact of boards of directors and corporate governance on a company's financial performance. Providing more clear evidence of positive financial returns from having an effective board or effective governance mechanism would convince companies to pay more attention to governance issues and take away the existing scepticism. However, this requires a more solid measurement of board effectiveness and more elaborated research models. Our study is a modest attempt to provide researchers with new measures and a renewed research framework.

A third avenue for further research on the effectiveness of boards is **longitudinal research**. It is generally accepted that longitudinal research strategies are better suited to study processes and patterns of change (Pettigrew, 1990). Our study was

limited to one period of time, resulting in a research framework whereby the board of directors is considered to be a social system. It was argued that board effectiveness results from a state or relative balance (or fit) between various structural and behavioural components. However, we believe that any stable fit between structure and behaviour is rather temporary and subject to change. In this respect, our study proposes an alternative dynamic board model, contrary to the commonly applied static research models. The suggestion to study one or more cases over an extended period of time, will enable researchers to examine the way the effectiveness of boards evolves over time and to display the patterns in a successful execution of board roles as they change. In-depth longitudinal studies in which board task performance is followed over a longer time period are required to have solid proof and a better understanding of the dynamics of effective boards, especially of how 'ideal' board configurations may evolve. Moreover, this kind of research can provide us with enriched insights into the changes that signal a serious decline or increase in board performance.

Fourth, further research could be aimed at exploring the value-added of **other determinants** for the effectiveness of boards. Our study has only extracted a limited number of variables from the literature but still other variables may be of importance to study in the context of boards of directors. We have already touched upon the need to examine the style and characteristics of the decision-making process. Moreover, the existence of power relationships inside the boardroom, the use of power and the leadership style of the chairman are also pointed out to be of particular relevance in the context of boards. In this respect, the (qualitative) studies of Pettigrew and McNulty (1998, 1995) have already shown how position, skill and will to use power sources, affects the contributions of non-executive directors to influence board behaviour on matters of substance. Leadership has also been identified by influential scholars as an important variable for group effectiveness (e.g. Hackman, 2002). From a corporate governance point of view, the discussion on board leadership structure has traditionally been focused on splitting or combining the roles of CEO and chairman of the board. In contrast, literature on group effectiveness has paid attention to leadership styles and how it influences the quality of the decisions. We suggest to further investigate how the decision-making style of a board's chairman may influence the

effectiveness of boards in performing their dual role set and what kind of leadership style is more appropriate when boards emphasize one role over the other.

A fifth avenue for further research is proposed by studying **board-management relationships**. Previous research on the relationship between the board of directors and the CEO has mainly focused on the division of power between these two anchors (e.g. Pearce and Zahra, 1991). The prevailing view underpinning empirical board research is the need for a board to control management by keeping sufficient distance from the CEO. The findings of our study have challenged this notion by documenting the need to develop a close working relationship with management for a successful execution of board roles. More empirical research could further investigate how the interplay between collaboration and control in the board-management relationship manifest itself for different role sets. For example, a study of Westphal (1999) has already shown how collaboration between top managers and outside directors, stemming from social ties in CEO-board relationships, enhance the provision of advice and counsel in the strategy-making process. In addition, researchers could empirically investigate how the coexistence of collaboration and control in the board-management relationship can trigger either positive or negative dynamics stimulating or hampering the effectiveness of boards. Research in this respect, could build on the work of Sundaramurthy and Lewis (2003), who developed a conceptual model illustrating the occurrence of dysfunctional board dynamics based on reinforcing cycles of collaboration and control. They suggest the paradoxical combination of trust and conflict as a vital means of enabling self-correcting cycles.

Finally, future research could focus more on **the individual level** instead of on the level of the board of directors. Research on the individual level could then concentrate on behavioural and/or psychological characteristics of the individual directors. Researchers could build on the work of Leblanc and Gillies (2005) who documented the existence of functional and dysfunctional director's types, based on three individual behaviour characteristics. Furthermore, we suggest further examining the cognitive styles of individual directors and their impact on how boards of directors perform their roles. The concept of cognitive styles, or the way individuals collect and process information, has been frequently studied in various settings and is suggested to influence the decision-making process within groups (Leonard et.al. 2005;

Bouckenooghe et.al., 2005). Research on board effectiveness has been concerned with constituting a board of directors with the appropriate mix of directors. Mainstream research has applied a rather narrow focus when studying the composition of the board of directors. Traditional operationalisations of board composition are closely connected with the measurement of director independence and dependence (Johnson et.al., 1996). The findings of our study have broadened this scope as they point to the fact that board effectiveness strongly depends on the competence and performance of the individual directors. Empirically investigating personality features of individual directors, which go beyond director independence and competence, would add an extra dimension to research on boards of directors and may enhance our understanding of how the effectiveness of individual directors contributes or hampers the effectiveness of boards.

To conclude, we must note that the list of the above mentioned propositions for further research is not exhaustive. They indicate only some of the promising avenues in board and corporate governance research. In fact, the extensions (theoretically, conceptually, methodologically and in sampling) that can be made to our research topic are nearly infinite, which stands in strong contrast to the often finite resources of a researcher. We have focused on the determinants of board effectiveness, examined the variables already indicated in the literature as highly relevant and studied these through the use of rich research strategies. This allowed us to find some interesting findings, leading to answers and new questions.

7.6 References

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8 APPENDICES

Appendix 1: code list

<i>FAMILY</i>	<i>CODES</i>	<i>OPERATIONAL DEFINITION</i>
DEBATE/DECISION-MAKING	occurrence	refers to the fact that discussions take place; no rubber-stamping
	quality	refers to the characteristics of the discussions such as neutral, objective, in-depth, open, critical, emotionless, based on facts, to the point
	contribution	relates to the participation in the discussions and the assumption that members contribute during the discussions (e.g. sharing of knowledge, information, ideas etc)
	decision	refers to the fact that decisions are taken
BOARD CULTURE	active involvement	refers to the fact that a board is interested and involved in the company; it takes initiatives, learns and contributes in contrast to a formal, passive board
	openness	refers to an open culture, the possibility or ability to express an opinion, transparency
	critical	refers to a critical attitude/behaviour
	common values or goal	refers to the fact that group members have a common denominator
	atmosphere-climate	relates to other unwritten rules or standards such as humour, a positive and constructive mind, professionalism, passion for excellence

INDIVIDUAL NORMS

commitment	refers to the fact that individual members are interested, involved and available (sufficient time)
preparation	refers to the fact that individual members are prepared (e.g. read the documents)
personality	relates to characteristics of the personality of individual members such as humility, ego, attitude, sense of responsibility, integrity, ethical
independence	refers to the courage of individual members to speak up and to show an independent mind

RELATIONSHIPS AMONGST THE BOARD MEMBERS

cohesiveness	refers to the chemistry and the fact that board members cohere
respect	refers to the fact that the board members respect each other
team	refers to the fact that board members operate as a team/group
trust	refers to the trust amongst the board members
contact	refers to the interaction, dynamic and the informal contacts between the board members

BOARD TASKS

context	refers to the conditions which are necessary to fulfil the tasks (e.g. delegation, position within the CG-tripod)
control	relates to the monitoring tasks a board is expected to fulfil (financial, legal, internal governance etc.)
strategy	relates to the involvement of the board in the strategic process
support	relates to the interaction of the board with its management (challenging, stimulating, sounding board, advising etc.)

BOARD-MANAGEMENT RELATIONSHIP

relationship with management	relates to the contact, symbiosis with and trust in management, as well as to the quality of management
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BOARD COMPOSITION

competence	refers to the fact that experienced, high-quality and competent members are sitting on the board
complementarity	refers to the fact that members complement each other
diversity	refers to the fact that members differ in background, views, experience, nationality etc.
mix	refers to the fact that various categories of directors are represented (executives, non-executives and independent directors)
size	relates to the limitation on the number of directors

OPERATIONS OF THE BOARD

meeting	relates to the characteristics of the board meeting such as frequency, timing, presentations, minutes
preparation	refers to the fact that the board meeting should be well-prepared in terms of agenda and information provided to the members
chairmanship	relates to the quality and role of the chairman of the board

Appendix 2: case study protocol

TABLE OF CONTENTS

- A. Introduction to the case study
 - A.1. Purpose of the case study
 - A.2. Theoretical framework for the case study

- B. Data collection procedure
 - B.1. Name of the site to be visited, including contact person(s)
 - B.2. Data collection plan
 - B.3. Expected preparation prior to the interviews

- C. Themes in written questionnaire
- D. Case study questions

A. INTRODUCTION TO THE CASE STUDY

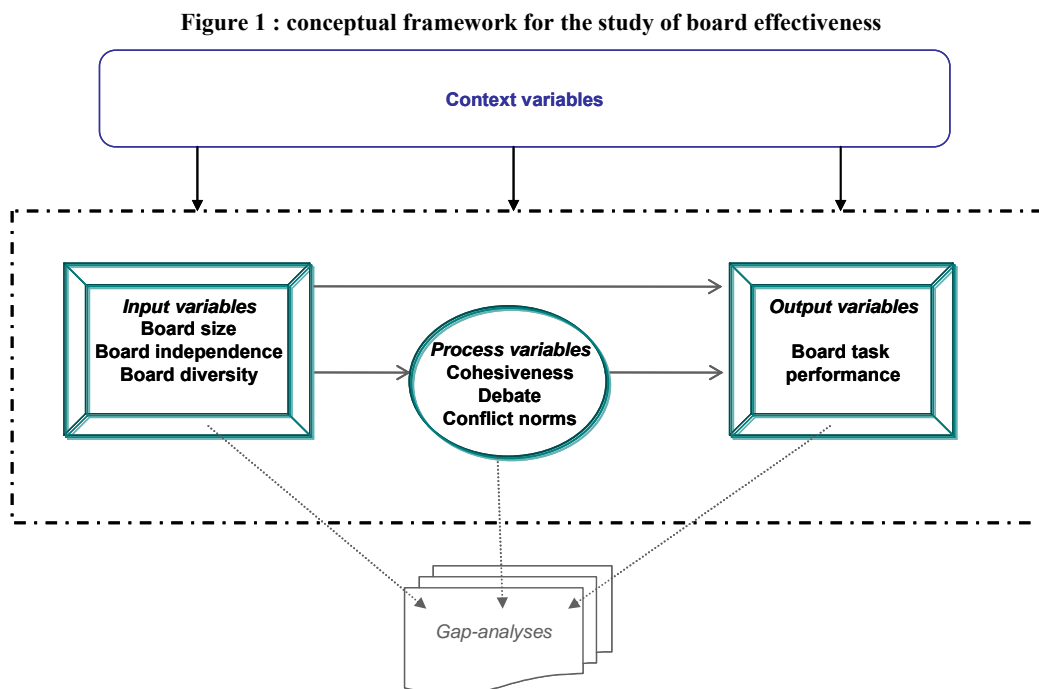
A.1. Purpose of the case study

The overall purpose of the case study is to examine the determinants of board effectiveness. The main research question to be addressed is: *how do board processes influence the task performance of boards of directors?* We will focus on the more intangible and behavioural aspects of board conduct. The objective is to get a better understanding of how structural and non-structural factors are interconnected to form a complex set of interrelated criteria which actually shape the effectiveness of boards in performing their key tasks.

The case study fits within the project of board evaluation the Company has decided on. As a listed company, the Company is subject to the Belgian Corporate Governance Code and has agreed to assess its board of directors. The Company's main goal of introducing an evaluation process is to come to a more performant "output" of the board, in line with the best practices on corporate governance in Belgium.

A.2. Theoretical framework for the case study

The research framework, underlying the case study, follows the input-process-output approach and strongly relies on the corporate governance literature as well as on the literature on group effectiveness. The central thesis is that board effectiveness is concerned with the outcomes of the board of directors and that these outcomes are directly and indirectly influenced by the make up of the board and by specific board processes. Figure 1 illustrates the research framework.



B. DATA COLLECTION PROCEDURES

B.1. Name of the site to be visited, including contact person(s)

Board of Directors (composition September 2005): 17 members – one vacancy

Table 1: composition of the Company's board of directors

<i>Name</i>	<i>Category</i>	<i>Directors since</i>	<i>Term expires</i>	<i>Language</i>	<i>Gender</i>	<i>Age</i>
Director A	executive	2003	01/03/2009	F	Male	50
Director B	NED-MS*	2004	01/03/2009	N	Male	52
Director C	NED-MS	1994	23/12/2006	N	Male	54
Director D	NED-MS	1996	23/12/2006	N	Male	39
Director E	NED-MS	1994	23/12/2006	F	Female	55
Director F	NED-MS	1994	23/12/2006	F	Male	57
Director G	NED-MS	2003	30/09/2009	F	Male	59
Director H	NED-MS	1994	23/12/2006	N	Male	59
Director I	NED-MS	1994	23/12/2006	N	Male	52
Director J	independent	2004	AGM 2010	F	Male	61
Director K	independent	2004	31/12/2006	F	Female	45
Director L	independent	2004	AGM 2010	E	Male	51
Director M	independent	2004	31/12/2006	F	Male	65
Director N	independent	2004	31/12/2006	N	Male	62
Director O	independent	2004	31/12/2006	E	Male	63
Director P	independent	2004	31/12/2006	N	Male	52
Director Q	independent	2004	AGM 2010	N	Female	53
<i>One vacancy**</i>	<i>independent</i>					

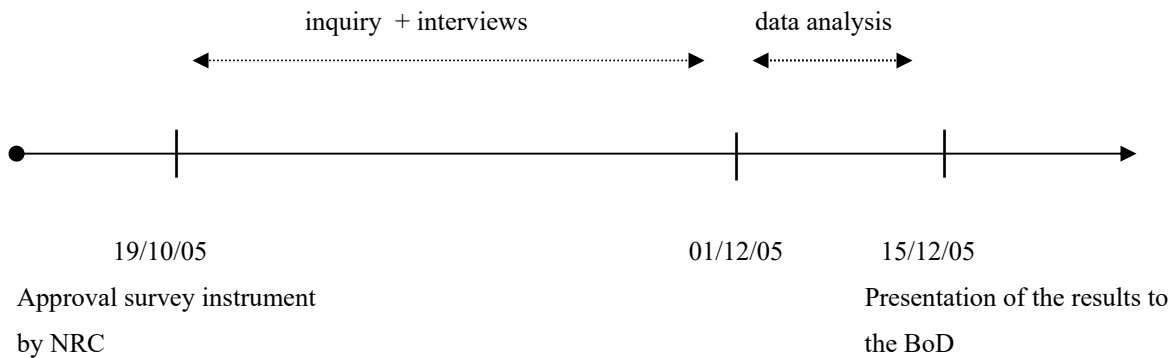
* NED-MS denotes non-executive directors representing the major shareholder

** the vacancy for one independent director has not been filled after the departure of director

B.2. Data collection plan

In performing the field research, multiple sources of evidence or the technique of *data triangulation* will be used. Field data will be collected using a self completion questionnaire completed with individual interviews. The latter will be done by the researcher, assisted by the Company Secretary, and will take place during October and November 2005. All the board members will be involved. The results of the evaluation project must be presented to the board of directors in December.

✚ Time frame



✚ Survey instrument

The self completion questionnaire is the result of a continuous interaction between the researcher and the Company. The survey instrument must meet the requirements of the case study as well as serve the particular objectives of the board evaluation project. Consequently, the questionnaire covers issues that are of relevance to both parties. In order to minimize potential biases in the responses -due to the different national languages-, the questionnaire is written in English.

The questionnaire must be approved by the Company's Nomination and Remuneration Committee in its meeting of October 19th. Once approved, the Company Secretary will send the questionnaire to all its board members. The individual responses serve as an input for the interviews. The processing and the analysis of the overall survey data will be done by the researcher.

✚ Individual interviews

The researcher and the Company agreed to use *focused* interviews, in which each board member will be interviewed for one to 1^{1/2} hours. Focused interviews are –to some extent- of an open-ended nature (=asking about a fact or manner as well as opinions about events) and assume a conversational manner but in fact the investigators follow a certain set of questions derived from this protocol.

The interviews will be held in the director's mother tongue. (Note: the interviews will not be recorded)

Interview data will be processed and analysed by the researcher. The results of both sources of evidence (inquiry and interviews) will be reported back to the Company in an anonymous way.

Schedule

Name	Interview date	Location	Time	Comments
Director A	25/11/05	Brussels	8.30-10.00	Questionnaire ok
Director B	2/12/05	Brussels	11.30-12.30	Questionnaire ok
Director C	1/12/05	Brussels	16.00-17.00	Questionnaire ok
Director D	24/11/05	Antwerp	14.30-16.00	Questionnaire ok
Director E	17/11/05	Brussels	14.00-16.00	Questionnaire ok
Director F	18/11/05	Brussels	11.00-12.30	Questionnaire ok
Director G	18/11/05	Brussels	15.30-16.30	Questionnaire ok
Director H	29/11/05	Hasselt	10.00-11.00	Questionnaire ok
Director I	30/11/05	Brussels	9.00-10.00	Questionnaire ok
Director J	25/11/05	Brussels	14.30-16.00	Questionnaire ok
Director K	/	/	/	Questionnaire ok
Director L	24/11/05	Telephone call	10.00-11.00	Questionnaire ok
Director M	24/11/05	Brussels	11.30-13.00	Questionnaire ok
Director N	17/11/05	Brussels	15.30-18.30	Questionnaire ok
Director O	10/11/05	Telephone call	15.30-16.30	Questionnaire ok
Director P	18/11/05	Deseldonk	13.30-14.30	Questionnaire ok
Director Q	9/11/05	Ghent	9.30-11.00	Questionnaire ok

B.3. Expected preparation prior to interviews

The following reading materials are proposed in preparing for the interviews:

General background information

Being a SA under public law, the Company operates in a highly regulated environment. In studying the board of directors it is useful to get insight into the legal context. In this perspective, Law 21 March 1991²², the Company Law, and the Articles of Association are recommended.

²² Wet betreffende de hervorming van sommige economische overheidsbedrijven

✚ Corporate governance information

The annual report and the website of the Company incorporate a separate corporate governance chapter. In addition a Corporate Governance Charter is currently being developed. Other relevant documents include the Charters of the various Board Committees.

✚ Board information

Two previous evaluations of the board of directors have taken place: (i) an introduction round by the chairman in October/November 2004 and (2) an analysis on the Company's Corporate Governance Structure by a law firm in February 2005. A summary of the results can be found in the Company's Briefing Note (5 July 2005).

C. THEMES IN WRITTEN QUESTIONNAIRE

- Composition of the board
- Relationships between the non-executive directors
- The functioning of the board of directors
- The information you receive as a board member
- Role and mission of the board
- Relationship between the board and the shareholders
- Relationship between the board and management
- The board's culture
- Board committees

D. CASE STUDY QUESTIONS (additional for interviews)

Reminder: the questions formulated below are supplementary to the statements in the written survey. Depending on the individual answers, some aspects will be more emphasised and discussed in-depth.

The questions in this protocol serve as a guide for the interviews and occur at two levels:

LEVEL 1 : this level relates to the questions asked to specific interviewees and reflects the *verbal* line of inquiry

LEVEL 2 : this level relates to the questions asked in relation to the individual case and these questions are posed to the investigator. They reflect the *mental* line of inquiry

Note: to understand the difference in levels, think about a detective. The detective has in mind what the course of events in a crime might have been (Level 2) but the actual questions posed to any witness or suspect (Level 1) do not necessarily betray the detective's thinking.

General

Level 2 : What determines an effective board?

Level 1: If a director serves on several boards of directors in different companies, ask the director to think of a 'good' board and a 'bad' board. What are the 3 (or 5) most important features of the 'good' board? Similarly, what are the 3 (or 5) most important features of the 'bad' board?

Level 2: Is the Company's board of directors an effective board?

Level 1 : How does the board of the Company compare with other boards you serve on (or have served on)? Would you think of the Company having a 'good' or 'bad' board? What are the strengths of the board? Similar, what are the major weaknesses? What aspects of the board could be improved?

Role of the board

Level 2 : Do the board members share a common vision on the role of the board?

Level 1: What is the most important role of the board of directors? Is the board fulfilling that role? In what ways should the board's role be expanded or reduced? What are the factors that influence the extent to which the board performs its role?

Level 2 : Does the board have a clear understanding of its responsibilities?

Level 1 : How involved is the board of directors in the strategy process? How involved *should* it be? If you think of recent important strategic decisions, has the board been involved too much/too little?

How involved is the board of directors in monitoring the company and the CEO/management? How involved *should* it be? Do you feel the expression "being in control" applies to the board?

Is the supervision of management in proportion to the delegated authorities (does the board monitor what it delegates)? Are the board's methods of measuring management performance sufficient/adequate?

What is the role of the committees in this respect? How do they contribute to the performance of the board's tasks?

Board discussions and decision-making

Level 2 : Does the board draw on the diversity of its members to make decisions that optimize its performance?

Level 1: How do you perceive the quality of the discussions? Is there a difference between the discussions that take place in the board versus those in the committees (remark: only relevant for committee members)?

Is each board member participating? Is each board member being heard? Do the discussions and decisions sufficiently benefit from the potential of the present board?

Is the board acting independently in the discussion/decision-making or are the discussion/decisions being influenced/dominated by specific “interests” or persons?

Are “hidden agenda’s” part of the discussion/decision-making?

Board culture

Level 2 : How do ‘intangible’ aspects such as culture, climate and the relationship amongst the directors influence board effectiveness?

Level 1: Is there openness in the board? Do certain (thorny) issues have to be discussed outside the board room? Are board members at ease to express their own views (even if they deviate from the majority)? Does this low/high degree of openness have an impact on the way the board performs its tasks? Would a change in the composition of the board, change the climate in the board?

How would you describe the relationship amongst the (non-executive) directors? Is there sufficient cohesion and chemistry? Does this have an impact on the way the board performs its tasks?

Role of the chairman

Level 2 : How does the chairman influence the working of the board?

Level 1: How would you describe the role of the chairman? Does the chairman stimulate or hinder a climate of constructive dissent? Does the chairman put a stamp on the decision-making?

Appendix 3: questionnaires

EXAMPLE OF THE FIRST QUESTIONNAIRE (in Dutch)

BOARD EFFECTIVENESS

Hieronder vindt u een lijst met tien stellingen. De stellingen omvatten diverse aspecten die de doeltreffendheid van de raad van bestuur kunnen beïnvloeden. “*Board effectiveness*” wordt daarbij gedefinieerd als “de mate waarin de raad van bestuur zijn strategische en controlerende rol vervult”. Deze stellingen zijn gebaseerd op een uitgebreide literatuurstudie en eerder uitgevoerd kwalitatief onderzoek. **De bedoeling is dat u volgende stellingen naar belangrijkheid rangschikt in dalende orde (1 MEEST belangrijk – 10 MINST belangrijk).**

OPDAT DE RvB ZIJN STRATEGISCHE EN CONTROLERENDE ROL ZOU KUNNEN VERVULLEN IS HET BELANGRIJK DAT	RANGORDE
Er in de RvB zowel leden van het management, onafhankelijke bestuurders als vertegenwoordigers van de aandeelhouders zetelen	10
De bestuurders goed voorbereid zijn	5
Alle bestuurders actief deelnemen aan de discussies	4
De bestuurders constructief kritisch ingesteld zijn	3
Er vertrouwen is tussen de raad van bestuur en CEO/management	9
De voorzitter consensus nastreeft	1
De informatie voldoende en tijdig is	2
Afwijkende visies getolereerd worden	8
Er complementariteit is op vlak van achtergrond, expertise en ervaring	7
De bestuurders goed met elkaar opschieten	6

Uw e-mail :

EXAMPLE OF THE SECOND QUESTIONNAIRE (in Dutch)

BOARD EFFECTIVENESS : DEEL 2

Hieronder vindt u een lijst met tien stellingen. De stellingen omvatten diverse aspecten die de doeltreffendheid van de raad van bestuur kunnen beïnvloeden. “Board effectiveness” wordt daarbij gedefinieerd als “de mate waarin de raad van bestuur zijn strategische en controlerende rol vervult”. Deze stellingen zijn gebaseerd op een uitgebreide literatuurstudie en eerder uitgevoerd kwalitatief onderzoek. **De bedoeling is dat u, vanuit uw bestuurservaring, aangeeft welke aspecten in de praktijk het meest voor verbetering vatbaar zijn. Gelieve deze in dalende volgorde te rangschikken (1 MEEST voor verbetering vatbaar – 10 MINST voor verbetering vatbaar).**

	RANGORDE
De informatie is voldoende en tijdig	5
De bestuurders zijn constructief kritisch ingesteld	6
De bestuurders zijn goed voorbereid	1
Alle bestuurders nemen actief deel aan de discussies	4
Complementariteit op vlak van achtergrond, expertise en ervaring	2
Er is vertrouwen tussen de raad van bestuur en CEO/management	8
De voorzitter streeft consensus na	9
Afwijkende visies worden getolereerd	7
Mix management, onafhankelijke bestuurders en vertegenwoordigers van de aandeelhouders	3
De bestuurders kunnen goed met elkaar opschieten	10

Uw e-mail :

Appendix 4: detailed analysis of themes

Table A: detailed overview of elements of theme 1

<i>Board composition</i>	<i>Number of respondents who mentioned this element</i>	<i>% of respondents (N=104)</i>	<i>Frequency this element is reported</i>
Diversity	30	28,85%	N=31
Complementarity	27	25,96%	N=27
Competence	25	24,04%	N=25
Mix (executive/non-executive)	10	9,62%	N=11
Size	7	6,73%	N=7
Total	99	95,19%	N= 101

Table B: detailed overview of elements of theme 2

<i>Board culture</i>	<i>Number of respondents who mentioned this element</i>	<i>% of respondents (N=104)</i>	<i>Frequency this element is reported</i>
Openness	17	16,35%	N=17
Active involvement	15	14,42%	N=15
Atmosphere-climate	11	10,58%	N=12
Common values or goal	6	5,77%	N=7
Critical	4	3,85%	N=4
Total	53	50,96%	N= 55

Table C: detailed overview of elements of theme 3

<i>Operations of the board</i>	<i>Number of respondents who mentioned this element</i>	<i>% of respondents (N=104)</i>	<i>Frequency this element is reported</i>
Preparation	23	22,12%	N=27
Chairmanship	18	17,31%	N=18
Meeting	8	7,69%	N=9
Total	49	47,12%	N= 54

Table D: detailed overview of elements of theme 4

<i>Board tasks</i>	<i>Number of respondents who mentioned this element</i>	<i>% of respondents (N=104)</i>	<i>Frequency this element is reported</i>
Strategy	15	14,42%	N=17
Support	9	8,65%	N=9
Context	5	4,81%	N=6
Control	5	4,81%	N=5
Total	34	32,69%	N= 37

Table E: detailed overview of elements of theme 5

<i>Debate/decision-making</i>	<i>Number of respondents who mentioned this element</i>	<i>% of respondents (N=104)</i>	<i>Frequency this element is reported</i>
Quality	10	9,62%	N=11
Occurrence	10	9,62%	N=10
Contribution	5	4,81%	N=5
Decision	3	2,88%	N=3
Total	28	26,92%	N= 29

Table F: detailed overview of elements of theme 6

<i>Individual norms</i>	<i>Number of respondents who mentioned this element</i>	<i>% of respondents (N=104)</i>	<i>Frequency this element is reported</i>
Personality	9	8,65%	N=10
Commitment	8	7,69%	N=10
Independence	6	5,77%	N=6
Preparation	2	1,92%	N=2
Total	25	24,04%	N= 28

Table G: detailed overview of elements of theme 7

<i>Relationship amongst the board members</i>	<i>Number of respondents who mentioned this element</i>	<i>% of respondents (N=104)</i>	<i>Frequency this element is reported</i>
Cohesiveness	8	7,69%	N=8
Contact	5	4,81%	N=5
Team	5	4,81%	N=5
Respect	3	2,88%	N=3
Trust	2	1,92%	N=2
Total	23	22,12%	N= 23

Table H: detailed overview of elements of theme 8

<i>Board-management relationship</i>	<i>Number of respondents who mentioned this element</i>	<i>% of respondents (N=104)</i>	<i>Frequency this element is reported</i>
Relationship with management	6	5,77%	N=7
Total	6	5,77%	N= 7

Appendix 5: frequency tables

Table I: frequency table of importance ranking scores for the full sample (N=150)

Determinants of board effectiveness	1*	2	3	4	5	6	7	8	9	10**
The board of directors includes a mix of executives, independent directors and non-executives representing the shareholders	24,0%	11,3%	5,3%	6,0%	8,7%	7,3%	8,7%	8,7%	8,7%	11,3%
The board members are well-prepared	8,7%	12,7%	18,7%	18,7%	16,7%	10,7%	7,3%	5,3%	1,3%	0,0%
All directors actively participate in the discussions	4,0%	4,7%	10,7%	11,3%	12,0%	12,0%	12,7%	13,3%	12,7%	6,7%
Board members show a constructive critical attitude	10,7%	18,7%	16,0%	18,0%	8,0%	16,0%	6,7%	3,3%	1,3%	1,3%
Trust between the board of directors and CEO/management	25,3%	12,0%	13,3%	8,0%	8,0%	9,3%	10,7%	7,3%	4,7%	1,3%
The chairman seeks consensus	2,0%	2,0%	3,3%	2,0%	7,3%	7,3%	16,0%	16,7%	31,3%	12,0%
The information is sufficient and on time	5,3%	14,0%	13,3%	12,0%	16,0%	13,3%	9,3%	8,7%	4,7%	3,3%
Divergent opinions are tolerated	3,3%	2,7%	8,7%	12,0%	12,0%	15,3%	14,0%	19,3%	11,3%	1,3%
Complementarity with respect to background, expertise and experience	15,3%	20,0%	10,0%	10,7%	10,7%	7,3%	10,7%	8,0%	5,3%	2,0%
Board members get along very well	1,3%	2,0%	0,7%	1,3%	0,7%	1,3%	4,0%	9,3%	18,7%	60,7%

* score 1 denotes 'item is most important'

**score 10 denotes 'item is least important'

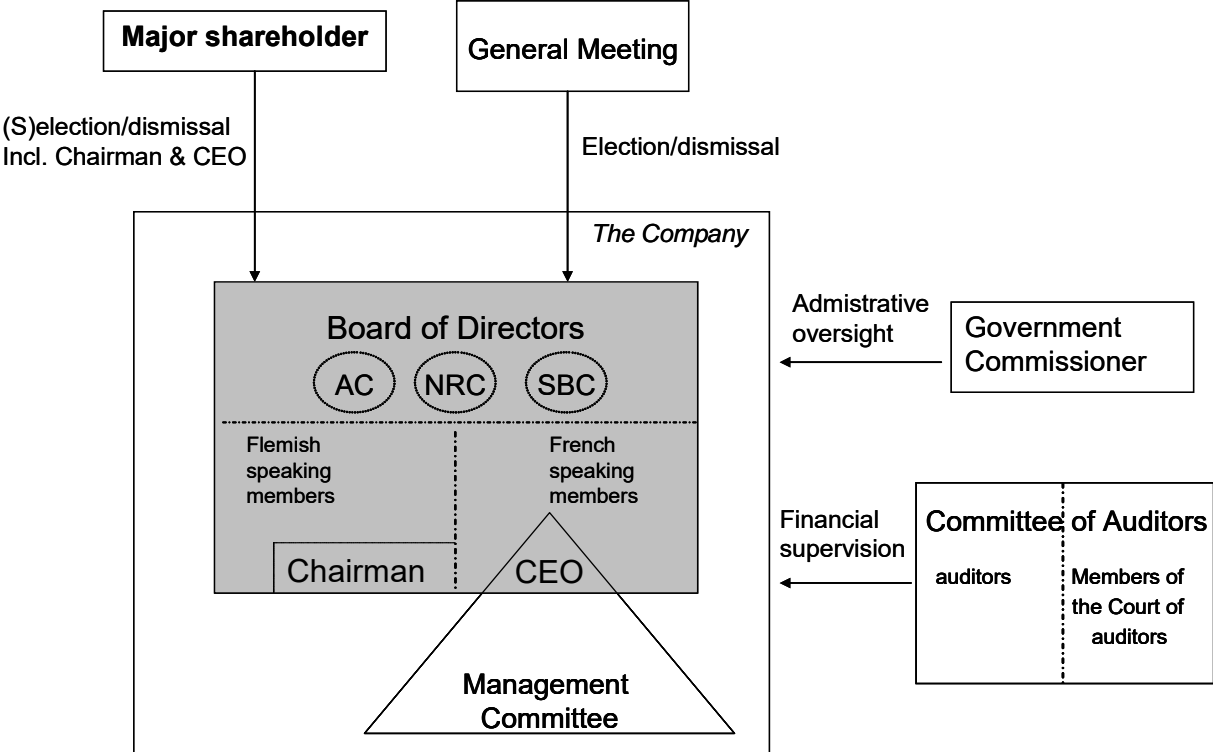
Table J: frequency table of corrigible ranking scores for the full sample (N=75)

Determinants of board effectiveness	1*	2	3	4	5	6	7	8	9	10**
The board of directors includes a mix of executives, independent directors and non-executives representing the shareholders	13,3%	6,7%	8,0%	6,7%	4,0%	6,7%	9,3%	10,7%	18,7%	16,0%
The board members are well-prepared	20,0%	25,3%	18,7%	12,0%	12,0%	6,7%	1,3%	0,0%	2,7%	1,3%
All directors actively participate in the discussions	8,0%	14,7%	20,0%	20,0%	4,0%	10,7%	9,3%	6,7%	4,0%	2,7%
Board members show a constructive critical attitude	4,0%	9,3%	14,7%	21,3%	13,3%	13,3%	8,0%	8,0%	2,7%	5,3%
Trust between the board of directors and CEO/management	0,0%	5,3%	5,3%	4,0%	10,7%	8,0%	21,3%	16,0%	20,0%	9,3%
The chairman seeks consensus	0,0%	2,7%	5,3%	1,3%	16,0%	13,3%	12,0%	14,7%	16,0%	18,7%
The information is sufficient and on time	29,3%	17,3%	10,7%	5,3%	13,3%	4,0%	5,3%	5,3%	5,3%	4,0%
Divergent opinions are tolerated	6,7%	4,0%	4,0%	8,0%	12,0%	18,7%	20,0%	14,7%	10,7%	1,3%
Complementarity with respect to background, expertise and experience	17,3%	13,3%	10,7%	16,0%	12,0%	12,0%	2,7%	8,0%	4,0%	4,0%
Board members get along very well	1,3%	1,3%	2,7%	5,3%	2,7%	6,7%	10,7%	16,0%	16,0%	37,3%

*score 1 denotes 'item needs most improvement'

** score 10 denotes 'item needs least improvement'

Appendix 6: the Company's corporate governance model



AC = Audit and Compliance Committee
 NRC = Nomination and Remuneration Committee
 SBC = Strategic and Business Development Committee