



Full length article

European board structure and director expertise: The impact of quotas



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ARTICLE INFO

Article history:

Received 12 July 2016

Accepted 13 September 2016

Available online 22 September 2016

JEL classification:

G34

G38

J16

Keywords:

Corporate governance

Board composition

European economy

ABSTRACT

This paper examines the relationship between the presence of female board members and measures of board independence and director expertise in Europe. We examine public corporations in countries that introduce gender quotas as well as those in a sample of countries without quotas. As shown in earlier papers, the quotas increase the percentage of females on the board; we also find pending quotas are associated with greater female board representation. We find some evidence that female representation is associated with greater board independence in the Nordic countries, but a legislated but not yet enforced quota decreases this positive association. In Southern Europe female representation is positively related to board expertise but the pending gender quota decreases this relationship. The paper provides empirical evidence that the composition of the board varies based on the gender of directors, but not to a great extent. This paper also reveals that pending and required quotas affect board structure.

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1. Introduction

The pervasive gender inequality on corporate boards has been in the news and on the agenda of lawmakers around the world. In Europe, leaders in several countries have proposed mandatory quotas for gender equality on corporate boards. Norway is the leader in legislated gender equality on boards of directors with a requirement of 40% of each gender since 2008 (Pande and Ford, 2011). Spain and France have also legislated quotas that were pending, with mandatory quotas to be implemented from 2015 and 2016 onwards, respectively (Pande and Ford, 2011). In addition to the strict quotas, many European countries also have recommendations for the minimum level of female representation in the corporate boards. While we expect the legislative quotas to increase gender equality on boards, especially in countries where they are enforced, it may also cause boards to be populated with unqualified members and a less than optimal proportion of insiders on the board.

While earlier studies show increased wealth from board diversity (see e.g., Carter et al., 2003) overall, the gender diversity of boards is commonly very low. Forty percent of the largest public corporations in the world have no women on boards according to the 2011 *Women on Boards Report* (Governance Metrics International, 2011). The European Union (EU) adopted a Gender Equality Strategy in 2010, with a goal of getting more women into senior positions in business life (EU, 2010, 2011a).

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Since the recommendation of gender equality has not caused significant changes, the EU is now considering legislative action in order to improve gender equality in the boardrooms (EU, 2011b).

Does the outside pressure for gender equality on boards enhance or detract from board quality? While studies show that diversity on U.S. boards enhances value (Carter et al., 2003), this diversity came from companies voluntarily adding members. We expect nominating committees to choose board members based on their expertise and perceived value added to the board. However, Withers et al. (2012) summarize the board selection literature and show several authors find director selection also is based on social process, often influenced by the CEO. With a large shock to the director selection process, such as the government enforcing gender quotas, the nominating process will change. Assuming boards are nominated for economic reasons prior to the quotas, the nominating committee now may be forced to choose board members who do not optimize board structure. On the other hand, if prior to quotas board members are chosen for social reasons, enforced gender diversity may lead to opening the board to more qualified members.¹ Societal pressure has been documented to impact the nominations of females to top corporate positions (Gregorič et al., 2015). Facebook is an example of a company faced with public pressure to add a female to its all-male board of directors who added an insider female to the board, thereby reducing the influence of outsiders on their board (Raice and Lublin, 2012).

In this paper, we study the relationship between female representation on the board and board independence and expertise using a sample of large public corporations from European countries from 2000 to 2011. Our paper is unique in that the sample includes two sets of European countries with quotas and without. One set of companies is the Nordic countries: Norway, with a female quota, and economically similar countries: Finland, Sweden, Iceland, and Denmark. The second set of companies is from Southern Europe: Spain and France with pending female quotas on boards and economically similar countries: Greece, Italy,² and Portugal. (Pande and Ford, 2011).

We examine how female representation on boards is affected by the quota recommendation (pending quota) and enforcement (required quota), as well as gender inequality within the country. Rather than measuring performance due to female board representation and quotas, we measure board structure and expertise. Using principal component analysis, we create two board factors. The first factor is independence based on outside representation of board members and lack of CEO duality. The second is expertise based on board member's education and professional certifications, number of previous boards sat on by board members, and board member networks. We perform a simultaneous system analysis that examines the relationship between female representation and these board factors. The regressions also examine how country-specific quotas (both pending and required), affect both female representation and board expertise and independence.

We find the relationship between board characteristics and female representation depends on the region and the specific board characteristic examined and the model specification. In the Nordic countries, female representation does not affect board expertise, but board independence is positively associated with female percentage. The pending and required female board quotas have little effect on board expertise or independence. In Southern Europe, where there is less female representation on corporate boards, both the presence of females and the quotas affect board characteristics. Female representation increases board expertise but does not affect independence, and both board independence and expertise reduce female representation. Finally, our findings indicate that the pending quotas decrease board expertise, but do not have a statistically significant impact on board independence.

Our research is unique in studying the effects of European boards' gender structure on board characteristics, given the quotas on board gender equality being passed by legislatures. The findings may therefore provide useful information for politicians in making the decision on whether mandating quotas on boards of directors is an effective strategy. Moreover, this study contributes to the existing literature by exploring the relationship between country-level variables and corporate board structure.

2. Literature review and hypotheses

In this section, we summarize the literature on corporate governance and female board representation. In addition, we develop hypotheses based on this literature.

2.1. Board composition: gender, independence and board expertise

2.1.1. Gender Diversity

Earlier literature has documented that including females on the board may improve governance practices of a firm (see Post and Byron (2015) for a summary of the literature). For instance, Adams and Ferreira (2009) suggest that gender-diverse boards invest more in monitoring. They further report that, in general, the women are more diligent in participating the board meetings than men, and that the more gender diverse the board is, the fewer attendance problems the male executives have. In a similar vein, Nielsen and Huse (2010) find that the presence of female board members is positively associated

¹ For a complete review of board selection articles, see Withers et al. (2012).

² In 2011 Italy introduced a boardroom gender quota, which requires public limited companies and state-owned companies to have at least 33% of each gender on their boards by 2015 (European Commission, 2013).

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