SESSION 1: BOARD OF DIRECTORS

THE COMPOSITION OF BOARD COMMITTEES IN FAMILY FIRMS: DOES OWNERSHIP MATTER?

Paolo Agnese [*], Francesca Romana Arduino [**]

[*] Faculty of Economics, International Telematic University "UNINETTUNO", Rome, Italy
[**] Department of Business and Management, LUISS University, Rome, Italy

How to cite: Agnese, P., & Arduino, F. R. (2022). The composition of board committees in family firms: Does ownership matter? In G. M. Mantovani, A. Kostyuk, & D. Govorun (Eds.), *Corporate governance: Theory and practice* (pp. 11–15). https://doi.org/10.22495/cgtapp1

Copyright © 2022 The Authors

Received: 19.04.2022
Accepted: 25.04.2022
Keywords: Board Committee, Corporate Governance, Family Firms, Family Ownership, Institutional Investors, Sustainability
JEL Classification: G23, G32, G34, Q56
DOI: 10.22495/cgtapp1

Abstract

Board committees perform many of the board of directors' functions, making informed decisions within the framework of delegated authority and providing specific recommendations to the board on the matters in their domain. Their composition draws significant attention from shareholders, as they represent the *locus* where important decisions are formally taken. The aim of this research is to investigate the role of ownership in designing the board committees in family firms, especially considering the recent quest for sustainable corporate governance that requires sustainability expertise in the board of directors. The relative importance of family owners and institutional investors may be moderated by the presence of family members in the firm management.

1. INTRODUCTION

In recent years, increasing attention has been paid to the activities of the board committees, that perform many of the most important board functions, such as the determination of remuneration policies, the identification of potential board members, and supervision of

financial reports. All this is due, among other things, to the increase in legal requirements and the growing complexity of the environment in which companies operate (Kolev, Wangrow, Barker, & Schepker, 2019).

As boards of directors have often been criticized for failing to fulfil their fiduciary duties, committees have been considered as a way to solve the board's deficiencies (Boivie, Bednar, Aguilera, & Andrus, 2016).

The importance of board committees and the fundamental contribution provided by non-executive and independent directors within the committees have been extensively analyzed by the literature on corporate governance (Kolev et al., 2019; Spira & Bender, 2004).

Some authors have focused on the link between corporate performance and board committee structure. For example, Klein (1998), regarding the board committee composition, finds a significant relationship between firm performance and how boards are structured, although the author shows little association between firm performance and overall board composition.

Other scholars have devoted their research efforts to specific boards committees, such as the audit committee (Bruynseels & Cardinaels, 2014; Farber, 2005; Kalbers & Fogarty, 1998; Klein, 2002), the governance committee (Huang, Lobo, & Zhou, 2009) and the compensation committee (Conyon & Peck, 1998). For instance, Farber (2005) found that fraudulent firms had poor governance mechanisms, but after detection, they make improvements, such as by increasing the number of financial experts on audit committees.

Finally, some studies have investigated the common membership, i.e., the presence of the same directors in different committees, in most cases the audit and the compensation committees (Brandes, Dharwadkar, & Suh, 2016; Liao & Hsu, 2013). For instance, Liao and Hsu (2013) examined the determinants and consequences of common membership across the compensation committee and the audit committee in the US firms.

According to Garg, Li, and Shaw (2018), the appointments of directors to committees may be influenced by the lack of specific regulation for chair appointments and the lack of significant time to devote to chair appointment decisions, thus leaving room for different types of favoritism, such as nepotism or friendship ties, often associated to family firms.

Notwithstanding the extant interest in the corporate governance literature, the composition of board committees still lacks thorough investigation in the context of family firms, which are typically characterized by a high involvement of family members in both ownership and management of the firm.

Prior literature suggests that family firms are characterized by a long-term orientation, as families are emotionally tied to the firm and desire to pass on the business to the heirs (Corbetta & Salvato, 2004). Since the degree of family involvement in the business is motivated by

socio-emotional wealth considerations (Gómez-Mejía, Haynes, Núñez-Nickel, Jacobson, & Moyano-Fuentes, 2007) rather than purely financial ones, potential conflicts may arise with external investors, mainly interested in the firm financial performance.

Although family firms present quite varied ownership structures, they are usually characterized by a high degree of ownership concentration that affects governance structures and mechanisms.

In order to extend the prior literature on the role of firm ownership in influencing the composition of board committees in family firms, we aim at investigating whether the presence of family shareholders and institutional investors can influence the design of board committees.

In this regard, it is also important to question whether the presence of family members in the firm management has a role to play in moderating the effects of firm ownership on the composition of the board committees. In fact, prior studies focusing on board committee composition mainly analyze some directorial characteristics in terms of gender, tenure, type and occupation (Kesner, 1988), neglecting to consider whether the director is also a member of the family.

This study appears of particular interest especially considering the recent quest for sustainable corporate governance, which requires knowledge of sustainability from the board of directors. In fact, on the great waves of societal and political pressures, the governance agenda seems to be evolving rapidly towards increased attention to sustainable decisions and actions. In an attempt to meet this goal, some firms have decided to set up a specific sustainability committee.

Firm ownership may exert an important role in prioritizing sustainability-driven decisions, by influencing the composition of board committees.

2. RESEARCH METHODOLOGY

Aiming to perform our analysis, we use a sample of all family firms listed on the Italian Stock Exchange between 2010 and 2020. We rely on various sources to build our dataset. We collect board-level data from the annual corporate governance relations available on the Italian Stock Exchange website, we gather firm-level data from the Refinitiv Thomson Reuters database. Finally, for collecting data regarding the ownership structure, we use the information available on the Consob website (i.e., the Italian Stock Exchange regulatory authority).

As regards the variables included in our study, our dependent variable is represented by the composition of board committees. We use dummy variables accounting for the presence of the different committees (audit, remuneration, corporate governance, etc.) and we create a categorical variable to measure the functional expertise of the directors. As explanatory variables, we adopt the family ownership and the institutional investors ownership, and as a moderating variable,

we include the number of family members in the firm management. Finally, consistent with prior studies, we consider a set of control variables at the firm level (i.e., firm age, firm size, leverage, profitability) and at the board level (i.e., board size, board independence).

To perform our analysis, we use a quantitative research method and a longitudinal research design, including industry year dummy variables.

3. CONCLUSION

This study calls attention to the role of ownership structure in designing the board committees in family firms. In particular, our research seeks to extend the theoretical understanding of the relationship between firm ownership and the composition of the committees, also taking into consideration the intensity of the family's involvement in the governance of the business.

This research makes significant contributions to both theory and practice. Specifically, we contribute knowledge to the extant corporate governance literature, investigating the role of ownership in designing the board committees in family firms.

Furthermore, this study also has the potential to provide significant practical implications in board design, as it may offer suggestions as to which directors are eligible for committee positions. Due to the recent call for sustainable corporate governance, boards of directors are expected to enlarge their competences, including sustainability expertise.

Firm ownership may exert an important role in prioritizing sustainability-driven decisions, by influencing the composition of board committees. In this sense, the design of the committees allows to attract new talents and obtain specific skills by inviting those who possess them.

REFERENCES

1. Boivie, S., Bednar, M. K., Aguilera, R. V., & Andrus, J. L. (2016). Are boards designed to fail? The implausibility of effective board monitoring. *Academy of Management Annals*, *10*(1), 319–407. https://doi.org/10.5465/19416520.2016.1120957
2. Brandes, P., Dharwadkar, R., & Suh, S. (2016). I know something you don't know!: The role of linking pin directors in monitoring and incentive alignment. *Strategic Management Journal*, *37*(5), 964–981. https://doi.org/10.1002/smj.2353
3. Bruynseels, L., & Cardinaels, E. (2014). The audit committee: Management watchdog or personal friend of the CEO? *The Accounting Review*, *89*(1), 113–145. https://doi.org/10.2308/accr-50601
4. Conyon, M. J., & Peck, S. I. (1998). Board control, remuneration committees, and top management compensation. *Academy of Management Journal*, *41*(2), 146–157. https://doi.org/10.5465/257099

5. Corbetta, G., & Salvato, C. A. (2004). The board of directors in family firms: One size fits all? *Family Business Review, 17*(2), 119–134. https://doi.org/10.1111/j.1741-6248.2004.00008.x
6. Farber, D. B. (2005). Restoring trust after fraud: Does corporate governance matter? *The Accounting Review*, *80*(2), 539–561. https://doi.org/10.2308/accr.2005.80.2.539
7. Garg, S., Li, Q. J., & Shaw, J. D. (2018). Undervaluation of directors in the board hierarchy: Impact on turnover of directors (and CEOs) in newly public firms. *Strategic Management Journal*, *39*(2), 429–457. https://doi.org/10.1002/smj.2716
8. Gómez-Mejía, L. R., Haynes, K. T., Núñez-Nickel, M., Jacobson, K. J. L., & Moyano-Fuentes, J. (2007). Socioemotional wealth and business risks in family-controlled firms: Evidence from Spanish olive oil mills. *Administrative Science Quarterly*, *52*(1), 106–137. https://doi.org/10.2189/asqu.52.1.106
9. Huang, H., Lobo, G. J., & Zhou, J. (2009). Determinants and accounting consequences of forming a governance committee: Evidence from the United States. *Corporate Governance: An International Review*, *17*(6), 710–727. https://doi.org/10.1111/j.1467-8683.2009.00769.x
10. Kalbers, L. P., & Fogarty, T. J. (1998). Organizational and economic explanations of audit committee oversight. *Journal of Managerial Issues*, *10*(2), 129–150. Retrieved from https://www.jstor.org/stable/40604189
11. Kesner, I. F. (1988). Directors' characteristics and committee membership: An investigation of type, occupation, tenure, and gender. *Academy of Management Journal*, *31*(1), 66–84. https://doi.org/10.5465/256498
12. Klein, A. (1998). Firm performance and board committee structure. *The Journal of Law and Economics, 41*(1), 275–303. https://doi.org/10.1086/467391
13. Klein, A. (2002). Audit committee, board of director characteristics, and earnings management. *Journal of Accounting & Economics*, *33*(3), 375–400. https://doi.org/10.1016/S0165-4101(02)00059-9
14. Kolev, K. D., Wangrow, D. B., Barker, V. L., III, & Schepker, D. J. (2019). Board committees in corporate governance: A cross-disciplinary review and agenda for the future. *Journal of Management Studies, 56*(6), 1138–1193. https://doi.org/10.1111/joms.12444
15. Liao, C.-H., & Hsu, A. W.-H. (2013). Common membership and effective corporate governance: Evidence from audit and compensation committees. *Corporate Governance: An International Review*, *21*(1), 79–92. https://doi.org/10.1111/corg.12000
16. Spira, L. F., & Bender, R. (2004). Compare and contrast: Perspectives on board committees. *Corporate Governance: An International Review, 12*(4), 489–499. https://doi.org/10.1111/j.1467-8683.2004.00389.x