BUSY BOARDS: HOW DOES THE SIMULTANEOUS PARTICIPATION OF DIRECTORS IN MULTIPLE COMPANIES AFFECT THE BOARD'S ACTIVITIES?

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Abstract

We analyze the simultaneous participation of directors in multiple companies and its effects on boards' roles and activities. By sitting in multiple boards, directors may face time scarcity and they may be too busy to adequately perform their tasks. Using survey questionnaires about board's activities, which were directly sent to firms and their directors, this paper founds that busy boards are considered to be less active, less independent and less relevant to firms. Additionally, these boards are less committed to their responsibilities, such as hiring/firing the CEO and evaluating executives' performance. They also do not monitor the firm's risk properly. Our results present an insider perception of the board's roles and activities, which can be useful for market regulators and policy-makers.

Keywords: Board Of Directors, Directors, Roles Of The Board, Busy Boards, Board Interlocking, Corporate Governance

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Introduction

The activities and procedures of the board of directors are amongst the main elements that shape the quality of corporate governance practices in public companies. Academically, most of the corporate governance researches are based on public external data about the boards (e.g.: Hermalin and Weisbach (1991), Yermack (1996), Bhagat and Black (1999)). We believe it is necessary to develop more than a demography-outcome approach so that the implications of the board's characteristics in its performance can be fully understood. For this reason, we intend in this study to analyze, from an insider, deeper and quantitative approach, directors' activities and functions on the board.

This research employs two survey questionnaires, containing questions about the board activities and work style, answered by 122 executives and directors of 65 Brazilian listed firms. They present their insider perception of the board's roles and activities, which is confronted with firm's characteristics and governance structure.

Similar studies using survey questionnaires can be found in Hendry, Kiel and Nicholson (2010) and Jones, Marshall, Mitchel and Ramsay (2007).

The primary survey data was collected by Guerra (2009a) in a pioneer research in Brazil analyzing the activities and working style of the board. These answers were confronted with the board interlocking database from Santos, Silveira and Barros (2009), who identified in which companies the directors of 389 Brazilian listed companies used to work for. All data is from December 2008.

Following the definition proposed by Fich and Shivdasani (2006), we consider as a busy board those in which half or more of members participate in three of more companies' boards. The board interlocking and busy boards phenomena constitute a prominent research line in foreign studies (e.g.: Fich; White, 2001; Ahn; Jiraporn; Kim, 2010), although they are incipient in Brazil (Santos; Silveira; Barros, 2009; Mendes-da-Silva; Vidal, 2010). Although some studies report a positive effect of multiple seats on boards on sharing director's experience and bringing new resources to the firm, most of the empirical results points out a negative overall effect of busy boards.

This paper brings three contributions to the study of boards. Firstly, it analyzes the relationship between ownership type and structure, firm's characteristics and the composition of the board, showing evidence on how these factors interact and affect the firm's governance in listed companies in Brazil. Secondly, it identifies the roles performed by boards and how board's characteristics and firm's governance affect them. Thirdly, it brings evidence of how the simultaneous participation of board directors in multiple companies affects board roles and activities.

Our results indicate that Brazilian boards are largely dominated by controlling shareholders and the participation of independent directors is still below the recommendation of the Brazilian code of best practices (IBGC, 2009) and by several authors, among them, Saito and Dutra (2006), Black, Carvalho and Gorga (2008).

In line with previous findings from studies in Brazil (BLACK; CARVALHO; GORGA, 2008; KPMG, CEG, 2008), the accumulation of chairman and CEO positions is not a major problem in Brazilian companies. More critical is the concentration of power by the chairman, who in most cases are also the controlling shareholder himself or a relative to the controlling family. It is also relevant the frequency of CEOs being family members or relatives of the controlling shareholders.

Regarding the roles of the board, it was observed a predominance of activities related to the control role. The guidance[21] role is also relevant, confirmed by the number of committees. The role of service however is less relevant in the boards. The predominance of the control and guidance (strategy in his case) roles was also observed by Stiles and Taylor (2001) in the UK.

The presence of family members of the controlling shareholders in the positions of chairman of the board or CEO is related to greater relevance given the role of service.

The major gaps observed by respondents in relation to the activities of the board are: (i) not to direct matters of succession, (ii) not to monitor risks, (iii) not to actually decide on the company's strategy, (iv) not to monitor the performance of executives and the company, (v) not to establish contacts of interest to the company.

As main contributions, this paper is the first to our knowledge to analyze the roles of the Brazilian board of directors using primary data collected through questionnaires. Additionally, it provides an important insider view of the boards for a prominent emerging market. Policy strategies and corporate governance guidance can be derived by market regulators by this study. The results of this research may also contribute to future theoretical models of corporate governance that aim to be more inclusive and customized.

This paper follows this sequence: the section 2 presents a literature review, section 3 details the sampling method and tests procedures, section 4 describes our results and section 5 concludes.

1 Theory and International Evidence

Several academic studies and corporate governance codes highlight the importance of the board of directors. A subject of increasing attention by market practitioners, academics and regulators are the so-called interlocked boards and busy boards.

According to Fich and White (2001) the board interlocking can be defined as a situation in which one director occupies the board of two or more companies, establishing therefore a link between them. Fich

[21]The authors consider the guidance role as the one related to strategy and policies related activities of the board.

and Shivdasani (2006) find evidence that busy boards, those in which half or more of directors work for three or more companies, are poor monitors: they do not oversee properly the management and the higher the number of seats occupied by directors the weaker is the surveillance over the firm.

Similarly, Cooper and Unzun (2010) develop the Busyness Hypothesis, in which they test whether busy directors would employ less monitoring oversight on the management, compromising the firm's performance. Ahn, Jiraporn and Kim (2010) find evidence that busy boards tend to approve value-destroying mergers and acquisitions. The authors show evidence that when an acquiring firm has a busy board the abnormal stock return of the company is negative in front of the acquiring announcement. Ahn, Jiraporn and Kim (2010) argue that busy boards tend to accept value-destroying acquisition due to the lack of proper time to evaluate the decision-making.

An additional argument about the scarcity of time is brought by Jiraporn, Davidson, Ning and DaDalt (2008), whom identify that busy directors tend to be absent more often from board meetings. The introduction of Sarbanes-Oxley, that imposes more strict responsibilities for directors, presented a relevant impact on reducing directors' absence on board meetings.

In Brazil, Santos and Silveira (2007), identified that in 2005 40% of companies had a board of directors in which half of participants work for at least another company. The authors also found a negative effect of board interlocking on the firm's value. Mendes-da-Silva (2010) suggests that there is a high level of linkages between Brazilian listed companies, indicating that board interlocking is a frequent and wide spread phenomenon in Brazil.

International rules about directors' time availability

Regarding the regulation on directors' time availability, several codes of corporate governance around the world mention a restriction on the number of boards that one director can seat, like the *The New York Stock Exchange* (NYSE), for instance, which suggests that companies introduce a limitation on the number of boards that company's directors may sit. In a 1994 report, the *National Association of Corporate Directors* (NACD) recommended that executives and CEOs should not participate in more than three outside boards. In a 2008[22] document, NACD suggests that directors must show commitment and time availability to perform their duties adequately and recommends clear guidelines to encourage directors to limit their participation on multiple firms.

European codes present similar recommendations: the British code of corporate governance[23] suggests that directors must dispose of enough time to deliberate their decisions adequately. The code also establishes that boards should not accept that directors who also work as executives in other companies sit on the board of more than one other FTSE 100 firm. The Belgium code of corporate governance follows the same line by recommending that directors should not participate in more than five listed companies, in order to dispose of adequate time to their tasks.

In Brazil, the Code of Best Corporate Governance Practices from the Brazilian Institute of Corporate Governance (IBGC, 2009) suggests that directors should limit their participation according to their function. The code approaches the availability of directors' time to execute their tasks. It suggests that the shareholders meeting should establish the maximum number of boards one director can occupy. Other Latin American countries also address the busyness level of directors as an important aspect of corporate governance codes.

2 Sample and Methodology

This study uses statistical tests for correlating the questionnaire's answers and the busyness level of firm's directors. Specifically, we use two distinct measures of board busyness: (i) the percentage of directors who work for three or more companies at the same time and (ii) a dummy variable for indicating companies in which half of the board work for three or more companies. This approach is based on Fich and Shivdasani's (2006) proxy for busy boards. We also run tests of difference of means for two groups:

[22]National Association of Corporate Directors, Key Agreed Principles to Strengthen Corporate Governance for U.S. Publicly Traded Companies, 2008.
[23](*UK Corporate Governance Code,* 2010).

the first one with busy boards and the other for companies that do not fit this classification. Additional tests based on linear OLS regressions compare the percentage of busy directors on the board and the directors' answers on their activities and working style. Other firm's characteristics, such as size, profitability and ownership structure were not considered in our tests, which is a research limitation.

Both survey questionnaires were sent in 2008. The first one was answered by 65 listed companies in Brazil, regarding the characteristics of their boards and their work style. In the second questionnaire, 122 managers and directors presented their personal view on matters of boards' activities and working style. It is worth mentioning that in our not-random sample, 56% of companies were listed in BM&FBovespa's Novo Mercado or issue American Depositary Receipts (ADRs) in NYSE. This point may indicate these firms are committed to higher corporate governance standards than those required by law. In this sense, the companies willing to answer the survey questionnaire could be more inclined to better corporate governance practices.

For the director's busyness measure, we used the database provided by Santos, Silveira and Barros (2009)[24]. In order to calculate the number of seats occupied by each firm's directors, the authors gathered the names and ID numbers of all directors in 389 listed firms at BM&FBovespa, with available data for December 2008. All this information is primarily provided by the Brazilian Securities Commission. By crossing the director's names, the authors determined the average number of seats occupied by each director, considering for that all the listed companies in that year.

The interlocking and busyness measures of Santos, Silveira and Barros (2009) were crossed with the information extracted from the survey questionnaires of Guerra (2009a). These two variables were tested against the questionnaire's answers and both presented the same trends and similar conclusions.

The most part of analyzed companies belongs to superior corporate governance listing segments: 66% of them belong to the Novo Mercado and some of the others to the Level 1 and Level 2 of BM&FBovespa.

Regarding the 122 surveyed executives and directors, 52% of them had been elected by the controlling shareholders or at least had some sort of family relationship with them. Less than 30% of the board could be classified as independent members. In our samples, less than 10% of directors were elected by minority shareholders[25].

3 Results

This section presents the effects of directors' busyness on the board's activities and working style. It is worth noting that 10% of our sample (6 out of 65 firms) could be classified as having a busy board, according to our definition. Two facts may explain this proportion: (i) most of the companies in our sample are listed in the top corporate governance segment and they are inclined to show a higher attention to the commitment of directors; and (ii) this study does not consider the directorships held in private companies (since these firms do not disclose this information).

Two main procedures were applied in our tests: OLS linear regressions and the difference of means' test. Both methodologies present the same conclusions: the higher the percentage of directors working for multiple companies, the weaker is the full achievement of board's duties and responsibilities[26].

Our surveyed executives were invited to classify in a 1 to 6 scale how do their boards executed their activities. Higher values indicate better governance practices, as shown on Figure 1, which highlights

[24]Santos, Silveira and Barros (2009) do not eliminate interlockingevidences among companies from the same economic group. For this reason, directors who work for correlated companies would be interpreted in the same way as those who work for companies of different economic groups.

[25]It is worth remarking that a great deal of surveyed directors was elected by the firm's controlling shareholders due to the highly concentrated ownership structure existent in Brazil. This could eventually bias our results by influencing the answers of our questionnaire.

[26]All results presented in this study show statistical significance at the 10% level or less. Additionally, the results obtained by the linear OLS regressions are in line with the tests of difference of means.No divergence was found between the two methodologies.

eight activities among those researched by Guerra (2009a) that show significant statistical differences between the two groups (busy and not-busy boards).

Figure 1.1 to 6 scale of board's activities accomplishment

The image below presents the main questions analised in our survey questionnaire regarding board's activities. The grading scale increases as the board becomes more active and more involved in strategic matters. Therefore, a high grade tends to indicate a good performer board, while a lower grade tend to indicate more passive and less committed board. These questions were directly sent to 122 executives and directors of 65 Brazilian listed firms in order to capture their insider perception of the board's roles and activities.

The following results were found by comparing the average score obtained by the group of firms with busy boards against the average score of non-busy board's firms.
Our tests concluded that busy boards do not perform satisfactory several relevant duties, as summarized in the above list and the Figure 2.

- Busy boards are less engaged in hiring or firing the CEO.

Our survey asked directors and executives on how often the firm used to hire/fire the CEO. Our results point that the higher is the participation of directors in multiple companies, the less likely is to replace the CEO. This evidence is in line with the hypothesis that busy boards tend to be more passive and not good performers of its fundamental attributions.

- Busy boards are less inclined to approve the hiring (and dismissing) the executives according to suggestions of the CEO.

Busy boards do not supervise the selection of executives. Besides the importance attributed by codes of corporate governance best practices, the Brazilian Corporate Law[27] is straight in allocate directors as the ones responsible for choosing the firm's executives. A reasonable hypothesis is that in these cases, CEOs became more powerful and take these hiring decisions alone. If the board does not oversee the hiring process adequately, they might not be able to assure the firm has the right decision-makers and therefore the company might not be protected from value-destroying decisions.

- Busy boards are less prone to evaluate and monitor the performance of company's executives.

Our survey revealed that busy boards are not good monitors of firm's executives. This evidence is particularly critical since, according to the Brazilian Corporate Law, directors have the duty of monitoring the firm's executives[28]. Besides, this is a recommendation of several codes of best practices in corporate governance. Busy boards that do not oversee the management may expose the firm to unpredictable risks.

[27](Brazil, 1976).
[28](Brazil, 1976).

- Busy boards are less prone to guide succession matters for key-executives.

The existence of a clear policy of succession for key-executives is considered a good corporate governance practice. The results of our study indicate that busy boards take less care of succession matter in the firm, exposing the company to potential management blackouts.

- Busy boards tend to avoid being involved on the elaboration/approval of the code of conduct and the internal regiment of the board.

Busy boards are less prone to be involved in the elaboration and approval of the board's internal regiment and code of conduct. This is an additional evidence of passivity associated to busy boards in matters of corporate governance.

- Busy boards participate less in relevant decisions, such as acquisitions, divestments, capital structuring and dividends payout.

Busy boards are less engaged in participating of strategic decisions. A possible explanation for these results is that busy directors do not have enough time and dedication to be fully aware of these matters. So they would rather be absent of this sort of decisions. This result is in line with previous studies.

- Busy boards are bad monitors of the relationship between executives and related parties.

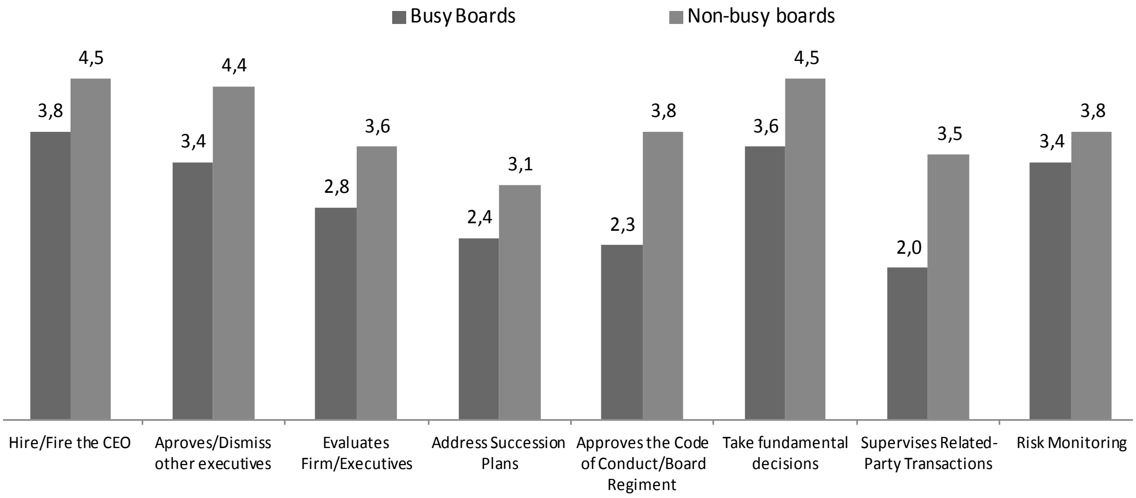
Busy boards do not perform a satisfactory oversight on the relationship of executives and related parties, in comparison to not-busy boards. Good corporate governance practices indicate the boards should not ignore the relationship between the firm and other parties, as it may lead to value-destroying decisions.

- Busy boards do not monitor adequately the firm's risks.

In line with the hypothesis of directors' busyness, firms with directors who work for too many companies tend not to monitor adequately the firm's risk, which may lead to losses. It is worth mentioning that, the 2008/2009 financial crisis, highlighted particularly how critical this factor is for the risk management in Brazilian firms. Guerra (2009b) suggests that the international crisis could lead to new thoughts on the board's role regarding risk management, which would enhance the adoption of voluntary corporate governance practices.

Figure 2, below, presents the average survey score regarding the questionnaire for each group of companies: those with busy boards and those which do not fit this category[29].

Figure 2. Characteristics associated to the participation of directors in multiple companies' boards



29All results are statistically significant at the 10% level, except the eighth test, about risk monitoring, which is significant at the 15% level. The linear OLS regressions present similar results. All conclusions must be interpreted carefully since there are no exogenous controls on this sort of tests.

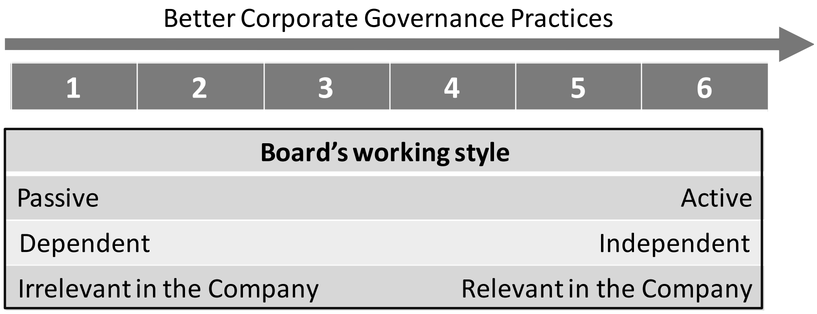
The chart presents the mean grade of answered by directors and executives in our questionnaire for each board activity (as describe in Figure 1). The results are segmented in two categories of companies in our sample: those with busy boards (those with more than a half of directors sitting in three or more companies) and non-busy boards (the remaining firms). The results indicate that non-busy boards are more active and perform better their tasks.

Among the activities compromised by the busyness of directors, three of them are listed among the major lacks of the board, as pointed out by executives in Guerra (2009a): do not address succession matters, do not monitor risks and do not monitor the CEO and other executives' performance.

3.1 Effects on the work style of board

The interviewees were asked to place their board between two semantic poles, according to the style and characteristics of functioning. Figure 2 shows the scale from 1 to 6, regarding the work style of the board.

Figure 3. Bipolar scale for the board's working style



The image below presents the main questions analised in our survey questionnaire regarding board's working style. The grading scale increases as the board becomes more active, independent and relevant for the company. Therefore, a high grade tends to indicate a good performer board, while a lower grade tend to indicate more passive and less committed board. These questions were directly sent to 122 executives and directors of 65 Brazilian listed firms in order to capture their insider perception of the board's roles and activities.

The following results were obtained by the comparison of each group's means: busy boards and not busy boards[30].

- Busy boards are associated to less active boards.

The survey's answers range in a scale from 1 to 6, being 1 equals to 'passive' and 6 to an 'active' board. Members of companies with busy boards tend to present lower answers.

One might speculate that directors who work for too many companies became too busy to perform their tasks, which may compromise their duties as a board member and the firm performance as a whole.

- Busy boards are associated to a lower level of board independence.

The higher the number of busy directors working in the company, the less independent the board is considered, according to survey's answers. This result suggests that for directors to perform independently they must not only fill the exigencies of corporate governance guidelines and recommendations, but also they must to be available and committed so their independence can result in a better functioning of the board.

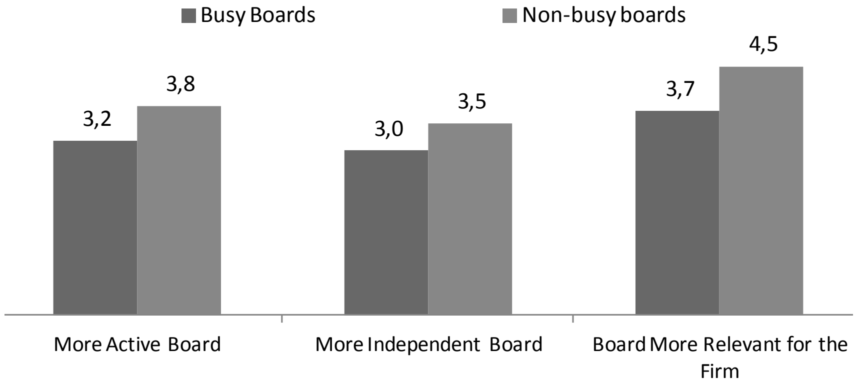
3) Busy boards are considered less relevant to their firms.

[30] The three tests are statistically significant for both the tests of means and the linear OLS regressions.

In line with previous results, firms in which directors are interlocked to multiple companies tend to have their boards considered as less relevant. This result strengths the evidence that a simultaneous participation of directors in multiple companies can compromise the favorable functioning of the board, affecting therefore the governance system as a whole.

A test of difference of means is presented in Graph 2. The grading score follows the same pattern previously explained: higher grades are associated to better corporate governance practices.

Figure 4. Effects of busy boards on board's activities



The chart presents the mean grade of answered by directors and executives in our questionnaire for each board working style question (as describe in Figure 3). The results are segmented in two categories of companies in our sample: those with busy boards (those with more than a half of directors sitting in three or more companies) and non-busy boards (the remaining firms). The results indicate that non-busy boards are more active, more independent and more relevant to their companies.

3.2 Effects on the board's characteristics

This section reports the results obtained by crossing the data on board interlocking and the answers of our survey questionnaire sent to 65 firms by Guerra (2009a). Here again the busyness of directors may impact in the board performance and attributions. The main results are described above:

The higher the number of board committees, the fewer the number of directors acting in multiple companies.

For this analysis, we split our sample in two subgroups: the first one composed by firms with more than 0.5 committee per director and a second group formed by firms with less than 0.5 board committee per director. By this division, the first category should represent firms with a higher demand of directors' time and engagement. The second group, with proportionally less committees, would by formed by firms that demand less from their directors.

Our results show that in the first group (more than 0.5 committee by director), only 8% of director were working for three or more companies (busy directors). On the other hand, for the companies with few committees (less than 0.5 committee per director) this ratio of busy directors goes up to 25%. This difference is statically significant at the 1% level.

Our results may indicate there is a direct correlation between the existence of board committees and the dedication of directors in deepening relevant matters in the company. This evidence is in line with international studies, such as Jiraporn, Singh and Lee (2009). The authors evaluate 1400 American companies and found out the involvement of directors in multiple boards significantly reduces their participation in boards' committees. Additionally, smaller boards, with a low number of members, tend to consume more time from their directors and therefore they present less participation in other firms.

1) *Companies that employ more face-to-face board meetings (than remote conference calls) are associated to a lower level of busyness by their directors.*

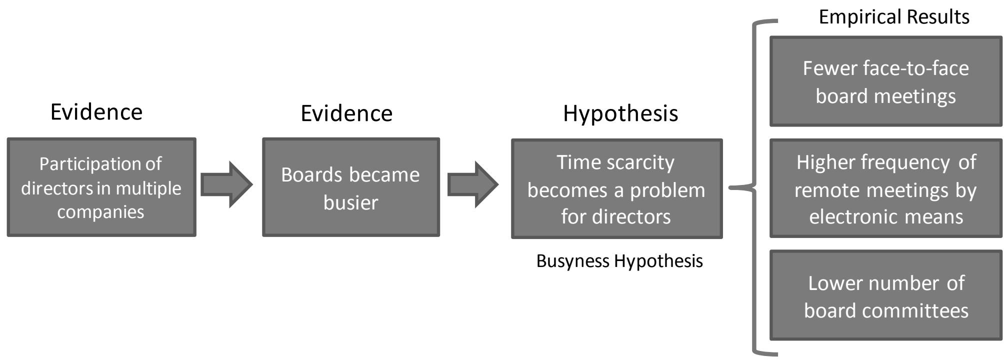
By answering Guerra (2009a) research, the 65 companies in our sample informed how many face-to-face and remote board meetings occurred in the previous year. They specified how many of them were conducted by means of conference calls, video and teleconferences.

The results indicate that a higher number of face-to-face meetings of the board are associated to a lower percentage of directors working for too many companies. The opposite is equally true: the higher the number of remote board meetings (by means of conference or video calls), the higher is the percentage of directors engaged in too many companies.

This evidence can be associated to how directors use their time: face-to-face meetings tend to demand more time and commitment by directors. On the other hand, firms which use remote conference means more frequently demand less time from their directors, allowing them to perform other activities in external firms. Codes of best corporate governance practices suggest that remote meetings should be use in a careful way, in order not to compromise the quality of board's functioning. Our evidence suggests that remote board meetings should be carefully watched when associated to board interlocking practices.

Similar results were found by Jiraporn, Davidson, Ning and DaDalt (2008), which identify that busy directors tend to be absent from board meetings more often than other directors.
Figure 5 summarizes the results of this section:

Figure 5. Hypothesis scheme for the effects of busy boards on board functioning



Visual scheme presenting our main hypothesis and empirical results derived from the survey questionnaire sent to 122 directors and executives in 65 Brazilian listed firms. Our evidence shows that by simultaneously participating in multiple companies, directors become too busy to perform adequately their tasks. Consequently, time scarcity becomes a problem for directors and the board well functioning. As presented in earlier sections, busy boards are classified as more passive, less independent and less relevant to their firms. Additional results bring evidence to corroborate these results: busy boards adopt fewer face-to-face meetings, have a higher frequency of remote meetings by electronic means (e.g. videoconferences) and have lower number of board committees.

4 Conclusions

The good functioning of the board of directors does not depend exclusively on its composition or its independence from the managers. The availability of time and dedication of directors is equally important for a good performance of the board. Multiple international studies show evidence that an excessive participation of directors in multiple directorships tend to have a negative effect on the company's management and in its market value. For this reason, codes of best corporate governance practices recommend restrictions to this practice.

In order to assess the impact of busy directors in board's activities, this study crossed data of two survey questionnaires fulfilled by 122 executives and 65 Brazilian firms about board's activities and work style with data on board interlocking and busyness measures.

This paper adopts the concept of busy boards, developed by Fich and Shivdasani (2006), which consider as busy those boards in which half of more of members work for three or more companies.

Our results indicate that busy boards seem to be less active, less independent and less relevant for their companies. Additionally, a higher participation of directors in multiple companies can compromise the performance of its main operations. Busy boards tend to deliberate less on firm's strategic decisions, tend to avoid taking decisions on hiring/firing the CEO and other executives, evaluate less the company's executives and do not monitor the firm's risks adequately. Busy boards oversee much less the relationship between the management and related parties, which opens a possibility for value-destroying decisions.

Additional results complement the hypothesis of time scarcity of directors: the higher is the participation of directors in multiple companies, the less frequent is the number of face-to-face meetings and higher is the probability of remote meetings, such as conference calls and videoconferences. In line with that, companies with less board committees present more busy directors than companies with non-busy directors. On the other hand, companies with a higher proportion of board committees tend to show directors more attached to their companies, with a fewer number of board interlocks.

This research presents a pioneer contribution in crossing data on board interlocking and primary data captured by survey questionnaires, addressed directly to executives and directors to understand board's activities and work style.

As main contributions, our evidences confirm the importance of recommendations of codes of best corporate governance practices regarding the board interlocking phenomenon. The Brazilian code, in its 2009 revision, attests that directors should restrain their participation in multiple companies. Additionally, the results can contribute for market agents and regulators regarding the definition of policies and recommendations on this important governance mechanism, the board of directors.

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