RELATIONSHIP BETWEEN QUALITY AND COMPETENCE OF SUPERVISORY BOARD ACTIVITIES AND CORPORATE GOVERNANCE

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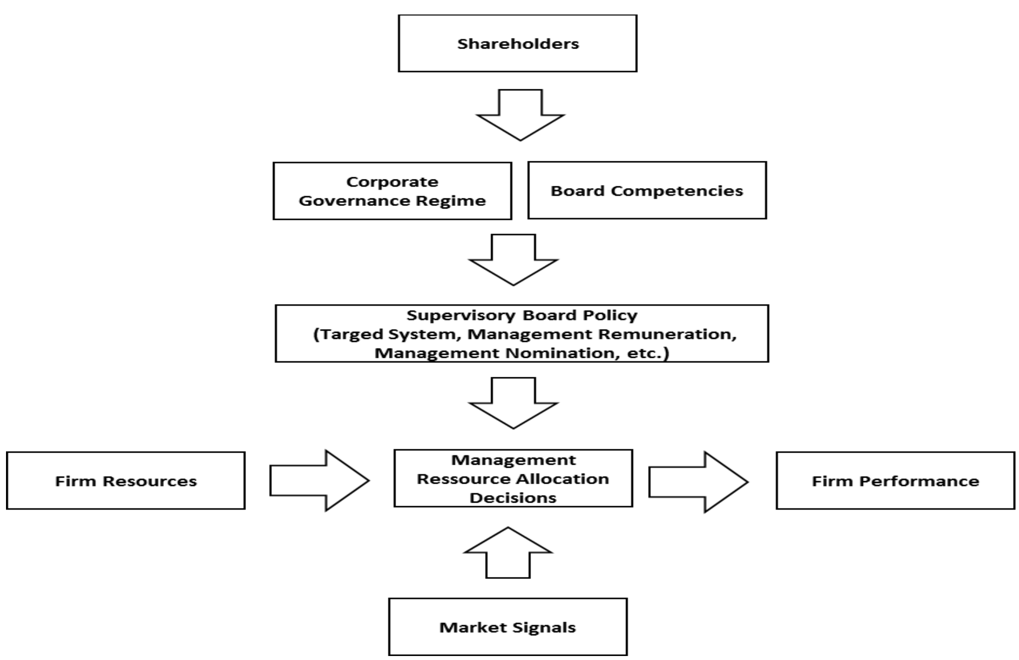
Abstract
According to the agency theory (Jensen & Meckling 1976), a positive relationship between corporate governance and company performance is expected to exist. This relationship is investigated in a study performed by the author of this paper. Two different approaches were chosen in parallel: (1) a quantitative data analysis, based on financial figures and corporate governance variables, and (2) a survey of supervisory board members of listed German companies. This paper is about the results of the structured interviews with 30 supervisory board members. The survey confirms that corporate governance regulations have an important influence on the quality of supervisory board activities and board competence. Many supervisory board members stated that the German Corporate Governance Codex leads to extended meeting time to fulfill regulatory requirements, more data requirements to identify and estimate risk issues and to rising risk awareness. The interview results converge with the result from the multivariate regression analysis.

Key words: corporate governance, firm performance, corporate performance, business performance, board structure, board competence,

Introduction

Firm performance is, in the framework of the theory of the firm, not simply a result of strategies and managerial activities but a result of a complex interplay between different institutions whose relationships are regulated in the corporate governance framework (corporate governance regime) and are shaped by the supervisory board competence and its institutionalized influence in terms of the corporate governance (see Figure 1).

Figure 1: Theoretical Model



(Source: Own presentation)

However, previous theories of the firm such as the market-based or the resource-based view observed and explained the firm on the management level and examine the degree of managerial impact which is, depending on the perspective, more or less restricted by the market or firm resources. Yet the restrictions of management inflicted by the institutional governance framework was only partially examined: The new institutional economics approach develops first propositions for a governance theory of the firm, but focuses more on transaction cost problems from the perspective of the owner, but do not confer its findings into the theory of the firm.

The overall objective of the author's study is to answer the following question: Do 'good' corporate governance and board competence explain firm performance differences? Two different approaches are chosen in parallel: (1) a quantitative data analysis, based on financial figures and corporate governance variables, and (2) a survey of supervisory board members out of this sample. The latter is subject of this paper.

Design of Survey

The survey is conducted by questionnaire-based interviews with 30 supervisory board members active in supervisory boards of the total sample's companies. The questionnaire contains questions with set answers (multiple choice) and without set answers. Questions without set answers are summarized through sorting the answers by topics and the evaluation of statements respectively by interpretation or citation of statements. The main characteristics of this sample are:

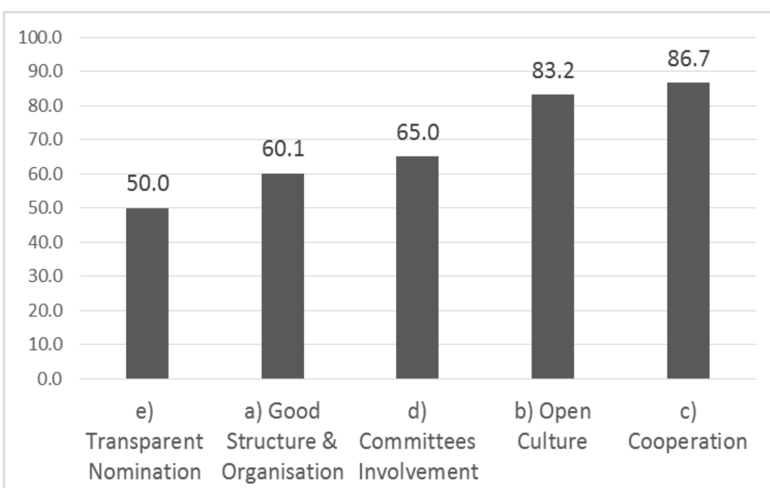
- 5 respondents out of the 30 respondents serve as supervisory board chairman.
- 5 respondents are female, 25 respondents are male.
- The average age is 61.6 years
- The average period of service as supervisory board member accounts for 14.4 years
- 97% of the respondents have served as CEO in the course of their professional life.

Results of Survey

1. Quality of supervisory board work:

The results let assume, that the sample's supervisory board members see board work quality, firstly, in the cooperation with the executive board, which is generally also the main task of the supervisory board by law and German Corporate Governance Codex. Items concerning the internal organization of board work are valued as less important. The supervisory board member nomination process is of minor importance (see **Hata! Başvuru kaynağı bulunamadı.**).

Figure 1. Relevance of Board Items (in %)

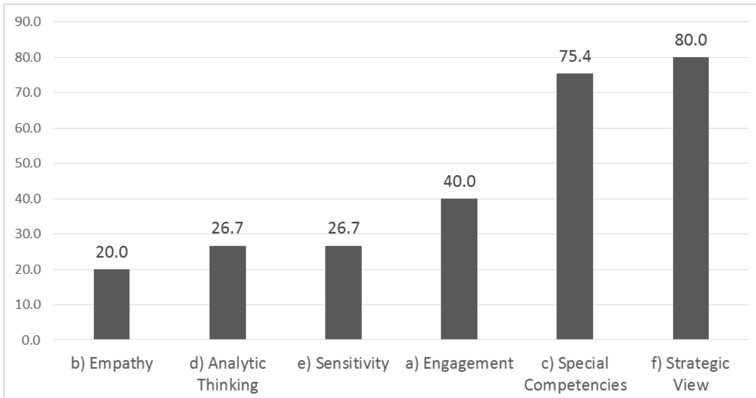


Source: Own calculation and presentation.

2. Personality traits a supervisory board member shall have to enhance the quality of work of the supervisory board:

The results show that formal competencies are less relevant instead of engagement and abilities such as special competencies and strategic view. It can be stated, that the majority of the respondents tend to prefer a mix of formal and informal characteristics regarding individual qualification while in the context of 'daily operations' of the supervisory board informal values are preferred. See Figure 2

Figure 2. Relevance of Supervisory Board Member Personal Traits (in %)

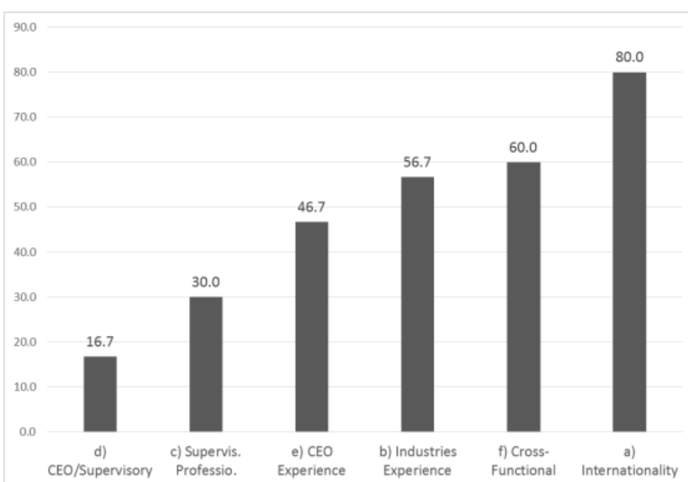


Source: Own calculation and presentation.

3. Personal and institutional competence:

The item "cross-functional experience" refers to experience in different corporate areas such as marketing, R&D, finance, etc. Interdisciplinary experience with an international background is the requirement with the most hits (see Figure 3). Instead, formal experience as a supervisory board member (item (c) and (d)) are not often required. Thus, the requirement ranking looks more than a CEO profile so that it could be stated, that the interviewed supervisory board members have a self-image, which resembles more to a CEO self-image. This is not really surprising, because all supervisory board members have long-term CEO experience. Furthermore the respondents refer stronger to soft skills and informal abilities than formal experience with supervisory board formalities such as supervisory board experience.

Figure 3. Competence Requirements for Board Members (in %)

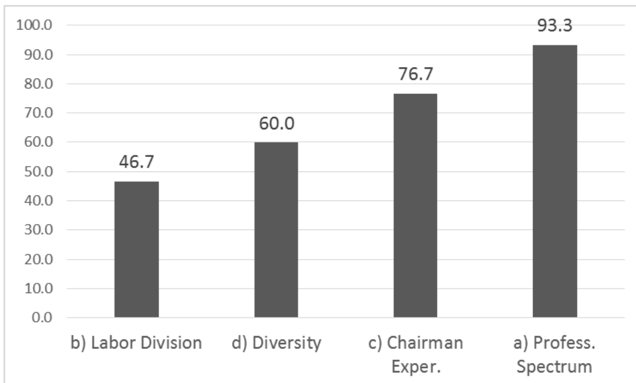


Source: Own calculation and presentation.

4. Supervisory Board competence as governing body:

The item “General Diversity” refers not only to gender diversity. However, the experience with the questionnaire in the survey leads to the assumption, that mostly gender diversity is associated with this term. Therefore, the interpretation of this value refers to gender diversity. The respondents weight the professional spectrum embodied in the supervisory board as extremely important with 93% (see Figure 4), which is the second highest approval rate measured in all questions. Furthermore, the chairman is seen as a central element in the supervisory board activities. Instead, even diversity is surprisingly valued higher than the division of labor through committee formation.

Figure 4. Supervisory Board Competence Characteristics (in %)



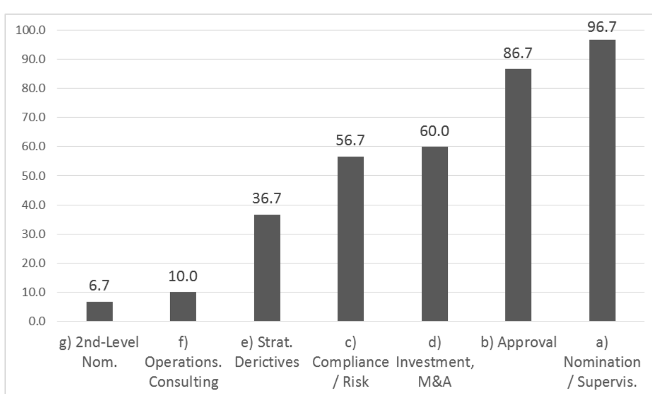
Source: Own calculation and presentation.

Thus the assumption gained from the preceding findings is that the informal factors outweigh the formal values such as labor division through committee formation, formal experience as a supervisory member, structure, and organization.

5. Most important tasks of the supervisory board:

The supervisory board member’s self-understanding of their role shows high formalism. While all other questions indicate a preference for informal items, the supervisory board members see their role as strictly formal with 96% approval rate concerning formal activities for nomination and supervision of the executive board (see Figure 5). Instead, strategic and operational issues were not seen as priority activities. Thus, it can be concluded, that tendency to informal abilities and processes does not mean, that the interviewed supervisory board members reject formalism. Rather, they distinguish clearly between necessary formalization and the regulatory framework requirements.

Figure 5. Activity Priorities of the Supervisory Board (in %)



Source: Own calculation and presentation.

6. How the supervisory board practice have changed in the last 10 years:

The answers regarding positive changes refer astonishingly often to the rising degree of formalization. Thus, one board member explains, that the supervisory board practice is more and more determined by standardized workflows due to the German Corporate Governance Codex, which applies, in particular, concerning risk and compliance issues. Here, the regulatory necessities lead to, on the one hand, more periodical reports and thus to a higher density of company data and information. On the other hand, these increasing corporate governance regulatory requirements lead to an information and formalization overload and to elevation of "approval barriers" along increasing liability risks. Thus, these statements reflect an ambivalence which exists also concerning the regulatory pressure regarding committee formation. One respondent mentions, that the rising number of committees and the rising intensity of committee work leads to better preparations of supervisory board decisions. Several respondents pronounce, that another effect of this excessive information circulation is, that the 'average' board meeting is much more informed and the discussion are based on more facts than before. One respondent mentions, that, several years ago, most of the board meetings were about gathering information from executives than on discussing essential issues. Furthermore, one member states, that the board Independency rules have led to the selection of new members based on their expertise and not based on their membership in a social network. Skills and experience are more sought-after. This leads to a higher diversity of knowledge and skills in the boardroom. Additionally, the nomination processes are much more transparent than years ago.

Conclusion

The survey reconfirmed that corporate governance regulations lead to more supervisory board process quality. While the members who are active in committees are increasingly better informed, supervisory board members without a membership in committees receive less information leading to a 'two-classes society'. This can lead, in the worst case, to a disproportionate communication effort. Increasingly, informal personal skills of supervisory board members are becoming relevant. Members are nominated more and more due to their complementary experience and knowledge. On the other hand, this search for special skills and knowledge takes much more time to find appropriate candidates than years ago. Several interviewed supervisory board members remarked explicitly, that the increasing liability risks strongly influence board work, in particular, concerning the direction of discussions, where more and more liability risks are discussed resulting in sometimes slowed decision-making.

Biography

Michelberger, Knut J.Doctoral Student at the University of Latvia, Faculty of Economics and Management, Riga, Latvia. Before joining the Doctoral Program at the University of Latvia, Knut served as Non-executive Director in several Private Equity sponsored portfolio companies and over many years as Director and CFO in various globally active companies based in Europe, USA and Asia and had initially studied mechanical engineering and business administration.

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