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Board Effectiveness in Small Firms
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Key words: Boards of directors; Small firms; Board effectiveness

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Board Effectiveness in Small Firms

Abstract

**Purpose:** This study investigates boards of directors in small firms and explores the link between board effectiveness and the composition, roles and working styles of the boards.

**Design/methodology/approach:** The study analyses data from a telephone survey of boards in 45 small firms. The survey included both the CEO and the chairperson of the board.

**Findings:** The study identifies three groups of small firms: ‘paperboards’, ‘professional boards’, and ‘management lead’ boards. Results show that board composition, board roles and board working style influence board effectiveness in small firms.

**Research limitations/implications:** Although the present study has found a link between board effectiveness and the role, composition and working style of boards of small firms, other potentially influential factors are also worthy of investigation; for example, the personal characteristics of the individuals involved, generational factors in family firms, and the situational circumstances of various firms.

**Practical implications:** The study reveals that, in practice, the management team and the board are substantially intertwined in small firms.

**Originality/value:** The main contributions are that the study explores how boards in small firms actually function and gives a detailed account of their composition and roles. More insight into this issue is important given the overemphasis within the governance literature on input-output studies using samples of large publicly-listed firms.

**Keywords:** Boards of directors; Small firms; Board effectiveness

Research paper
1. Introduction

If firms are to become and remain competitive, the board of directors must do more than perform the ‘control’ role described by Jensen and Meckling (1976); rather, it is becoming increasingly clear that the board must play ‘strategic’ and ‘service’ roles (Borch and Huse 1993; Fiegener 2005; Hendry and Kiel 2004; Ingle and Van der Walt 2001; Johnson, Daily, and Ellstrand 1996; Ruigrok, Peck, and Keller 2006; Stiles 2001). Boards of directors that adopt such roles can become platforms for active development of firms by becoming involved in strategic decision-making (Fiegener 2005; Hendry and Kiel 2004,) and the sharing of knowledge and experiences (Castaldi and Wortman 1984, Muth and Donaldson 1998, Stiles 2001). On a practical level, the ‘working style’ of such a board becomes more structured (Van den Berghe and Levrau 2004), decision-making becomes more efficient (Gabrielsson and Winlund 2000), and the board becomes a support and potential ‘sparring partner’ for the chief executive officer (CEO) (Westphal 1999; Zahra and Pearce 1989).

The purpose of this study is to investigate boards in small firms and to explore board effectiveness in terms of board composition, role and working style. According to Huse (2007) board effectiveness is accomplished when board members use information and their expertise to enhance creativity and coherence in the processes of decision-making and control. Thus, effectiveness does not imply the amount of resources used by the board, but the kind of resource the board constitutes for the firm. Effectiveness is consequently context-dependent.

Board effectiveness is dependent upon i) mechanisms, which refer to board composition; ii) standards, which refer to board task expectations and thus board role; and iii) actual board task performance, which refers to the execution of tasks or in other words, the working style of the board (Huse, 2007). Research on boards of directors tends to focus on structure (composition and role) rather than process. There have been several calls for research on actual board behaviour and the working processes of boards (Forbes and Milliken 1999; Huse 2000; Uhlaner et al. 2007). This paper presents an insight into actual board practice in a small firm.
context in contrast to the existing governance literature. As contended by Petrovic (2008), the prescriptive nature of corporate governance literature provides little guidance as to actual board functioning.

There has been a tendency for research into boards of directors to focus on large, publicly listed firms because data on such firms are easily available (Huse 2000; Uhlaner, Wright, and Huse 2007). Indeed, a large part of the research on so-called ‘small’ firms has examined firms with up to 500 employees (Daily and Dalton 1993; Fiegener 2005; Fiegener, Brown, Dreux, and Dennis 2000a; 2000b). From a European perspective, such research is not directly applicable to ‘small’ firms—because the definition of a ‘small firm’ according to the European Commission (as adopted for the present study) is a firm that has 10–49 employees. Empirical research on the boards of directors of such small firms is still in its infancy (Huse 2000). The ownership structure of such small firms is usually different from that of larger firms; in particular, many are family businesses (Corbetta and Montemerlo 1999), with the owner also being the manager of the firm (Gubitta and Gianecchini 2002). For these reasons, there are often no clear boundaries between owners/managers and the board of directors (Corbetta and Tomaselli 1996; Brunninge, Nordqvist, and Wiklund 2007; Uhlaner et al. 2007). This embeddedness makes research into this area complex and challenging.

The remainder of this paper is structured as follows. The next section presents a theoretical discussion on board effectiveness in relation to board composition, working style and roles. Thereafter, the methodology is described, the empirical findings are presented and discussed, and the conclusions of the study are drawn. Finally, limitations are acknowledged and suggestions for further research are presented.

2. Conceptual background

Much of the literature on boards of directors departs from the assumption that board composition influences board effectiveness (Johnson et al. 1996; Zahra and Pearce 1989). Board composition is generally related to i) the size of the board, and ii) the proportion of outside
directors on the board (Johnson et al. 1996; Zahra and Pearce 1989). The basic assumption is that a large board with a high proportion of outside directors performs the control, service and strategic roles in a more effective manner (Fama and Jensen 1983; Johnson et al. 1996; Zahra and Pearce 1989). On the other hand Huse (2007) states that small boards tend to apply a more efficient working style showing greater focus, participation and interaction. Research shows that many small firms have small boards and a low ratio of—if any—outside directors (Johannison and Huse 2000; Ward and Handy 1988). This is often explained in terms of the theory of ‘managerial hegemony’, whereby the owner/manager is seen as unwilling to cede power to the board (Pettigrew and McNulty 1995) and therefore prefers a ‘rubber-stamp board’ with no outside directors (Mace 1971). On the other hand, research reveals that a substantial number of small firms do have outside directors and consequently see some benefit in having them on the board (Fiegener et al. 2000a; 2000b). This can be explained in terms of resources: as the involvement of ‘outsiders’ in small firms often is directly linked to a need of counsel and specific expertise (Clarysse, Knockaert, and Lockett 2007). Consequently, the link between board composition and board effectiveness seems rather equivocal in a small firm context. It can be argued that because large and small firms operate in markedly different environments, the general prescriptions regarding composition may not be valid for ensuring the effectiveness of boards in small firms.

An effective board is involved in a variety of roles (Forbes and Milliken 1999), the main roles being the control, service and strategic role (Zahra and Pearce 1989). From the perspective of agency theory, the board of directors is the formal body for stakeholders (principals) to control managerial behaviour (agents) and thus the board has a control role (Fama and Jensen 1983). The service and strategic roles are generally related to the theory of ‘resource dependency’, which holds that a firm’s success is dependent on the firm possessing a range of internal and external resources (Pfeffer 1972). In accordance with this view, the role of the board of directors is to secure access to these resources by providing links between the firm and its environment (George, Wood, and Khan 2001). Indeed, the board itself can be seen as a
resource in the development of the firm. In adopting a service role, the board provides counsel to the CEO (Zahra and Pearce 1989), enhances the firm’s reputation and establishes contacts with stakeholders (Borch and Huse 1993). The strategic role of the board includes the development and implementation of vision, goals, and business plans. In a small firm context it has been found that the service and strategic roles of the board are perceived as more important than the control role (Daily and Dalton 1993; Gabrielsson and Winlund 2000; Van den Heuvel, Van Gils, and Voordeckers 2006).

Board effectiveness is more than the sum of its composition and roles; there is a need to consider not only what the board is and what the board does, but also how the board carries out the tasks assigned to it. An aspect of such board behaviour is the working style of the board. According to Gabrielsson and Winlund (2000) this concept includes i) the involvement of the board members (knowledge, skills, preparations, commitment, independence), and ii) board structures (formal board routines, formal board evaluations, frequency of meetings). Even though board behaviour is recognized as crucially important in ensuring the effectiveness of boards (Forbes and Milliken 1999; Gabrielsson and Winlund 2000, Zahra and Pearce 1989), research on the actual behaviour of boards—both in small and large firms—is scarce (Huse 2000). It is the contention of this study that board working style is an important indicator of board effectiveness in a small firm context.

3. Methodology

3.1 Sample and Data Collection

The selection of companies to be included in the present study was based on three criteria. First, the companies were all ‘limited’ companies (which, in Finland, are required by law to have a board of directors). Secondly, the companies all had 10–49 employees (in accordance with the European Commission’s definition of a ‘small’ firm). Thirdly, the boards of
the companies all had at least two permanent members (to ensure that some degree of ‘real’
board activity did take place).

Using these criteria, the sample was chosen from among small firms in Ostrobothnia—a
region on the West coast of Finland known for its entrepreneurial activity. At the time of the
study in 2006, the Ostrobothnian Trade Association included 65 member firms that fulfilled all
three criteria noted above. All of these firms were contacted, and 56 agreed to participate in the
study. However, 11 firms did not complete all parts of the questionnaire and were therefore
discarded from analysis. The final number of firms was therefore 45 and the response rate was
thus 69 percent.

To ensure a satisfactory response rate and high-quality data, the survey was conducted by
telephone. The telephone interviews varied in duration from 20 to 45 minutes. The interviews
followed the disposition of the questionnaire (see below for details), but many respondents also
shared additional information about their firms. This information, which was documented,
provided a qualitative understanding of the research problem that was utilised in interpreting the
findings of the survey.

The questionnaire consists of four main parts: (i) information about the firm (for example,
turnover, industry, number of employees); (ii) information about each of the board members
(for example, age, gender, education, specific competence, board tenure); (iii) information about
the respondent (for example, age, gender, education, specific competence, board tenure); and
(iv) information about the role and the working style of the board.

The questionnaire was answered by the CEO and the chairperson of the board. In 14 of
the total 45 firms that participated in the study, both CEO and chairperson of the board was the
same person. Thus, the study included totally 76 respondents. The majority of CEOs were
members of the board; indeed, only seven were not (but all of these stated that they still took
part in, and influenced, board activity). Table 1 provides information on the firms and boards
who took part in the study.
Table 1: Description of firms and boards

<table>
<thead>
<tr>
<th>Information about the firms</th>
<th>0-10 years</th>
<th>11-15 years</th>
<th>16-20 years</th>
<th>21-30 years</th>
<th>31-45 years</th>
<th>46- years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Age</td>
<td>6</td>
<td>5</td>
<td>5</td>
<td>9</td>
<td>8</td>
<td>12</td>
</tr>
<tr>
<td>Turnover</td>
<td>0.2-1.0 M€</td>
<td>1.1-2.0 M€</td>
<td>2.1-3.0 M€</td>
<td>3.1-4.0 M€</td>
<td>4.1-5.0 M€</td>
<td>5.1-10.2 M€</td>
</tr>
<tr>
<td>Number of employees</td>
<td>10 employees</td>
<td>11-20 employees</td>
<td>21-30 employees</td>
<td>31-40 employees</td>
<td>41- employees</td>
<td></td>
</tr>
<tr>
<td>Industry</td>
<td>Manufacturing</td>
<td>Construction</td>
<td>Wholesale &amp; retailing</td>
<td>Technical services</td>
<td>Logistics</td>
<td>Food</td>
</tr>
<tr>
<td></td>
<td>12</td>
<td>4</td>
<td>5</td>
<td>6</td>
<td>3</td>
<td>3</td>
</tr>
</tbody>
</table>

Information about the board

<table>
<thead>
<tr>
<th>Number of board members</th>
<th>2 members</th>
<th>3 members</th>
<th>4 members</th>
<th>5 members</th>
<th>6 members</th>
<th>7 members</th>
</tr>
</thead>
<tbody>
<tr>
<td>Age of board members</td>
<td>40 years</td>
<td>41-50 years</td>
<td>51-60 years</td>
<td>61-70 years</td>
<td>71- years</td>
<td>1</td>
</tr>
<tr>
<td>Board tenure</td>
<td>0-5 years</td>
<td>6-10 years</td>
<td>11-15 years</td>
<td>16-25 years</td>
<td>26- years</td>
<td>5</td>
</tr>
<tr>
<td>Education (number of boards)</td>
<td>Business</td>
<td>Technical</td>
<td>Industry-specific</td>
<td>Other</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>33</td>
<td>29</td>
<td>28</td>
<td>10</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

3.2. Measures

Board Effectiveness

Board effectiveness was measured on the basis of four variables. The first three of these variables were formulated as statements, to which interviewees were asked to respond on a four-point scale (1 = ‘completely disagree’ to 4 = ‘completely agree’). The fourth variable was a simple measure of the frequency of board meetings. The four variables can be summarised as follows:

* ‘The board exists only because of legal requirements’; this statement was derived from Mace (1948) and Ward and Handy (1988), who concluded that the only motivation for
having a board in small firms was because it was required by law. A board, which exists only due to such external requirements, is arguably not an effective board.

* ‘The board is an important means of developing the firm’; this variable was chosen to assess the opposite of the scenario reflected in the first variable.

* ‘The board is of value to me (CEO) when managing the firm’; adapted from Smith (1958) and Vance (1983). These authors discuss the fact that CEOs often prefer “rubber-stamp” boards and do not allow the board to participate in the management of the firm. Consequently, such a board cannot perform effectively.

* Number of board meetings per year; this variable was derived from Gabrielsson and Winlund (2000), who assert that the frequency of meetings is important for the board’s ability to perform its tasks effectively.

**Board composition**

Board composition was measured with four variables:

* Number of board members: adopted in accordance with Forbes and Milliken (1999), Gabrielsson and Winlund (2000), and Fiegener et al. (2000a).

* Average board tenure (years): adopted in accordance with Forbes and Milliken (1999).
  Measured as the sum of the tenure of all board members divided by the number of board members.

* Average age of board members (years): adopted in accordance with the view of Forbes and Milliken (1999); this measure on individual board members has not previously been used in empirical research, perhaps because data are not readily available (Huse 2000). Measured as the sum of the age of all board members divided by the number of board members.

* Board members’ relationships (family/relatives/owners/employees/external/other): in accordance with Combs et al. (2007), but contrary to Fiegener et al. (2000a), a member who had no other connection to the firm (other than being a board member)
was classified as ‘external’; the category of ‘other’ included customers, financiers, and the like. The other relationships are not mutually exclusive, but one member may have up to four relationships. In extant literature, board members’ relationship is most frequently measured as an insider/outsider ratio. Gabrielsson and Winlund (2000) and Voordeckers et al. (2007) question this measure as it is too vague. Fiegener et al. (2000a) apply a more detailed classification, where inside directors include family members (relatives of the owner/manager, whether employed in the firm or not) and managers. Outside members are divided into affiliated directors (directors with fiduciary relationships to the firm, such as bankers and lawyers), owners and non-owners. However, as Johannisson and Huse (2000) we detected that it was difficult to make a clear classification of insider/outsider directors. Therefore, instead of asking whether members were insiders or outsiders, the respondents were asked to state the members’ relationship to the firm.

**Board Roles**

The ‘control role’ of the board was measured with five variables, each of which consisted of a statement requiring a response on a 4-point scale (1 = ‘completely disagree’ to 4 = ‘completely agree’):

* The board actively controls the financial situation.
* The board actively controls the CEO.
* The board actively controls the implementation of strategies and plans.
* The board actively controls decision-making within the firm.
* The board actively controls the competitive situation of the firm.

The statements were all derived from Zahra and Pearce (1989).

The ‘service role’ of the board was measured with one variable—a statement requiring a response on a 4-point scale (1 = ‘completely disagree’ to 4 = ‘completely agree’):

* The board is an important ‘sparring partner’; derived from Zahra and Pearce (1989).
The ‘strategic role’ of the board was measured with one variable—a statement requiring a response on a 4-point scale (1 = ‘completely disagree’ to 4 = ‘completely agree’):

* The board contributes with visions regarding the development of the firm; derived from Stiles (2001).

Working Style of the Board

The working style of the board was measured with four variables. The first two were direct questions. The second two were statements that called for a response on a four-point scale (1 = ‘completely disagree’ to 4 = ‘completely agree’). The variables can be summarised as follows:

* Question: ‘Do board meetings have an agenda?’; adopted in accordance with Smith (1958), Zahra and Pearce (1989), and Gabrielsson and Winlund (2000).

* Question: ‘How many days in advance is the agenda distributed to members?’; adopted in accordance with the same authors.

* Statement for response: ‘Board meetings are characterised by a lack of discussion in dealing with items and making decisions’: derived from Zahra and Pearce (1989).

* Statement for response: ‘Board meetings deal primarily with routine items’; derived from George et al. (2001).

3.3. Data Analysis

Non-hierarchical cluster analysis using SPSS was adopted as the primary method of data analysis. A three-cluster solution (‘paperboard’, ‘professional board’, ‘management lead board’) was found to be most appropriate for representing the data with respect to ‘board effectiveness’.

This three-cluster solution was then tested with respect to ‘board composition’, ‘control role’, ‘service role’ and ‘strategic role’ as well as ‘working style of board’. Three methods of analysis were applied: (i) ANOVA; (ii) Kruskal-Wallis one-way analysis of variance; and (iii) Pearson’s chi-square test. In general, ANOVA and the Kruskal-Wallis test showed similar p-values. Kruskal-Wallis one-way analysis of variance was used as the number of observations in
the different clusters was small. Chi-square was applied when testing for differences when the variables were qualitative.

4. Findings and Discussion

4.1. Board Effectiveness Clusters

As noted above, the cluster analysis resulted in three clusters describing board effectiveness (see Table 2). The clusters were characterised as: (i) ‘paperboards’; (ii) ‘professional’ boards; and (iii) ‘management lead’ boards.

Table 2: Effectiveness clusters

<table>
<thead>
<tr>
<th></th>
<th>Paperboard</th>
<th>Professional</th>
<th>Mngt lead</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>( n=14 )</td>
<td>( n=8 )</td>
<td>( n=23 )</td>
</tr>
<tr>
<td>The board exists only due to legal requirements</td>
<td>4.00</td>
<td>1.13</td>
<td>2.13</td>
</tr>
<tr>
<td>The board is an important means in the development of the firm</td>
<td>1.79</td>
<td>3.63</td>
<td>3.30</td>
</tr>
<tr>
<td>The board is of value to me when managing the firm</td>
<td>2.07</td>
<td>3.63</td>
<td>3.35</td>
</tr>
<tr>
<td>Number of meetings/year</td>
<td>1.39</td>
<td>11.25</td>
<td>4.57</td>
</tr>
</tbody>
</table>

\( a \) Measured on the scale 1-4, where 1 = completely disagree, 4 = completely agree

The common characteristic of the first cluster was that of a ‘paperboard’. In this cluster the board existed only because of legal requirements (4.00). This cluster did not see the board as being a resource in the development of the firm (1.79) and was not inclined to view the board as being valuable for the management of the firm (2.07). Board meetings of these firms were held approximately once a year (1.39 times per year on average). These boards are clearly ineffective.

The second cluster consisted of boards of directors that were ‘professional’. They disagreed with the statement that the board existed only because of legal requirements (1.13). The board was considered a resource for management (3.63) and for the development of the firm (3.63). These boards met almost once a month (11.25 times per year on average). Boards in this cluster are characterised by effectiveness.
The ‘management lead’ cluster was neither a paperboard nor a professional board. The boards had a mid-range response of 2.13 (on a scale of 1–4) to the statement that the board exists only because of legal requirements. Boards in the third cluster were considered a resource for the firm (3.30), but not to the same extent as boards in the second cluster. Moreover, they were regarded as being of value in the management of the firm (3.35). Formal board meetings were held every quarter (4.57 meetings per year on average). Boards in this cluster are more effective than ineffective, however, not as effective as professional boards.

4.2. Board Effectiveness and Board Composition

As shown in Table 3, the statistical analyses revealed that the composition of the boards differed among the three clusters.

Table 3: Results of statistical tests

<table>
<thead>
<tr>
<th>Board composition</th>
<th>Paperboard</th>
<th>Professional board</th>
<th>Management-lead board</th>
<th>P-value a</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of board members</td>
<td>2.71</td>
<td>4.25</td>
<td>4.04</td>
<td>0.003/0.001</td>
</tr>
<tr>
<td>Board tenure (years)</td>
<td>19.24</td>
<td>12.90</td>
<td>15.03</td>
<td>0.186/0.117</td>
</tr>
<tr>
<td>Average age of board members (years)</td>
<td>54.74</td>
<td>47.56</td>
<td>49.91</td>
<td>0.086/0.117</td>
</tr>
<tr>
<td>Board members’ relation to firm b</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Proportion of internal boards (family only)</td>
<td>85.72 percent</td>
<td>25.00 percent</td>
<td>43.48 percent</td>
<td>0.064</td>
</tr>
<tr>
<td>Proportion of internal boards (non-family)</td>
<td>0.00 percent</td>
<td>25.00 percent</td>
<td>21.74 percent</td>
<td></td>
</tr>
<tr>
<td>Proportion of mixed boards (including external)</td>
<td>7.14 percent</td>
<td>50.00 percent</td>
<td>30.43 percent</td>
<td></td>
</tr>
<tr>
<td>Other board composition (for example, including financiers)</td>
<td>7.14 percent</td>
<td>0.00 percent</td>
<td>4.35 percent</td>
<td></td>
</tr>
</tbody>
</table>

Board role

<table>
<thead>
<tr>
<th>The board actively controls:</th>
<th>Paperboard</th>
<th>Professional board</th>
<th>Management-lead board</th>
<th>P-value a</th>
</tr>
</thead>
<tbody>
<tr>
<td>the financial situation c</td>
<td>2.29</td>
<td>3.75</td>
<td>3.17</td>
<td>0.004/0.005</td>
</tr>
<tr>
<td>the CEO c</td>
<td>2.00</td>
<td>2.63</td>
<td>2.61</td>
<td>0.185/0.128</td>
</tr>
<tr>
<td>the implementation of strategies and plans c</td>
<td>1.86</td>
<td>3.25</td>
<td>2.78</td>
<td>0.000/0.001</td>
</tr>
<tr>
<td>decision-making within the firm c</td>
<td>2.14</td>
<td>2.88</td>
<td>2.74</td>
<td>0.081/0.085</td>
</tr>
<tr>
<td>the competition c</td>
<td>1.86</td>
<td>2.50</td>
<td>2.65</td>
<td>0.066/0.065</td>
</tr>
<tr>
<td>The board is an important sparring-partner c</td>
<td>2.21</td>
<td>2.88</td>
<td>3.17</td>
<td>0.019/0.029</td>
</tr>
<tr>
<td>The board contributes with visions regarding the development of the firm c</td>
<td>2.29</td>
<td>3.38</td>
<td>3.00</td>
<td>0.024/0.039</td>
</tr>
</tbody>
</table>
**Working style**

<table>
<thead>
<tr>
<th>Description</th>
<th>Percentage</th>
<th>Percentage</th>
<th>Percentage</th>
<th>P-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>No meeting agendas at all/ do not send agendas in advance</td>
<td>64.29%</td>
<td>12.50%</td>
<td>39.13%</td>
<td>0.056</td>
</tr>
<tr>
<td>Board meetings are characterised by items being dealt with and decisions being made without discussion</td>
<td>3.43%</td>
<td>1.88%</td>
<td>2.77%</td>
<td>0.002/0.003</td>
</tr>
<tr>
<td>On board meetings are primarily routine items dealt with c</td>
<td>3.43%</td>
<td>2.00%</td>
<td>2.50%</td>
<td>0.003/0.005</td>
</tr>
</tbody>
</table>

**Firm characteristics**

<table>
<thead>
<tr>
<th>Description</th>
<th>Percentage</th>
<th>Percentage</th>
<th>Percentage</th>
<th>P-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Major development realised during past 3 years</td>
<td>7.10%</td>
<td>75.00%</td>
<td>40.00%</td>
<td>0.005</td>
</tr>
<tr>
<td>Turnover (million €)</td>
<td>2.13%</td>
<td>5.08%</td>
<td>3.04%</td>
<td>0.038/0.045</td>
</tr>
<tr>
<td>Age (years)</td>
<td>27.43%</td>
<td>40.63%</td>
<td>33.48%</td>
<td>0.343/0.424</td>
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<tr>
<td>Number of employees</td>
<td>18.86%</td>
<td>26.63%</td>
<td>25.22%</td>
<td>0.238/0.324</td>
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<tr>
<td>Industry</td>
<td>All represented</td>
<td>All represented</td>
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a P-values: if two values ANOVA/Kruskall-Wallis; if one value Chi-test  
b Chi-test conducted simultaneously across all three clusters and the four types of board composition. The number of observations in each category is too small to be interpreted as statistically significant. However, the observations in each cluster show clear tendencies.  
c Measured on the scale 1-4, where 1 = completely disagree, 4 = completely agree  

In firms in the first (paperboard) cluster, the members of the board were predominantly chosen from among family members and relatives. It is likely that such family members and relatives were recruited to the board to ensure that the board remained passive and that power remained concentrated to the CEO. Moreover, there is easy access to such members.

In contrast, the study found that in the second (professional) cluster board members were more likely to have been recruited from among shareholders or other persons external to the firm. External members were recruited to the board because CEOs wished to have an active board composed of people with heterogeneous knowledge and experience. These findings are in accordance with previous research (for example, Vance 1983), which suggests that the inclusion of external board members is associated with a range of advantages for the firm.

In the third (‘management lead’) cluster, the common arrangement was that boards mainly consisted of individuals with managerial or other responsibilities in the firm. In these cases, the board and the management team were virtually synonymous. These individuals worked daily side by side in the firm. This feature distinguished the third cluster from the two other clusters. The management team was considered to have the knowledge and experience to
handle the tasks traditionally assigned to the board, and there was no difference (or only minor differences) between the board and the management team.

The three clusters also demonstrated differences with regard to board tenure, the ages of board members, and the number of board members. As shown in Table 3, paperboards had the longest tenure, the highest average age, and the smallest number of members. It is likely that these findings reflected a general lack of interest: from its inception the board only exists due to external requirements. Thus, when the board is put together, as little effort as possible is devoted to it. In contrast, in firms with professional boards, it was considered desirable to have a board of diverse composition to ensure that it could contribute to the firm’s development. Board members were therefore recruited with care, evaluated, and (if necessary) replaced. The third (‘management lead’) cluster resembled the second (‘professional’) cluster with respect to board tenure, the ages of members, and the number of members. Board tenure was relatively short and the average age of members was relatively low. The latter was due to the fact that the board was often composed of two generations—with the older generation having established the firm and the younger generation looking to take it over. The number of board members in the third cluster reflected the structure of the organisation in terms of the number of ‘managers’ in the firm.

4.3. Board Effectiveness Related to the Role and the Working Style of the Board

As shown in Table 3, the findings from the statistical analyses revealed that both the working style of the board and the role ascribed to it differed between the first two clusters. In the ‘paperboard’ cluster, the boards could be described as having no real role. In contrast, in the ‘professional’ cluster, there was evidence of a strong control role and a strong strategic role (although the service role was only moderate). With regard to the ‘management lead’ cluster, the boards tended to resemble the ‘professional’ cluster to a greater extent than the ‘paperboard’ cluster.
As the statistical analyses in Table 3 show, the lack of an actual role among the ‘paperboards’ is partly explained by their working styles. This is in accordance with Gabrielsson and Winlund (2000), who showed that there is a significant positive relationship between working style and role (including service, strategic, and control roles). In the present study, the ‘paperboard’ cluster often had no agenda for their meetings, and board members thus had no opportunity to in advance acquaint themselves with the items that were to be discussed and decided upon. In some cases, the agenda was even written up after the actual meeting had taken place. In many cases, minutes were seldom kept; in other cases, minutes purported to record meetings that had actually never taken place. In addition, the few board meetings that actually did take place were mainly focused on routine items—such as signing the annual accounts. There was often no discussion on items; rather, they were simply approved in accordance with the CEO’s opinion.

In contrast, in the ‘professional’ cluster, boards met almost once a month; moreover, in general, the working processes of the boards were structured and systematised. The agenda was usually formulated and sent out in advance to board members. In addition, the meetings followed formal procedures and minutes were kept. The respondents from this cluster disagreed with the statements that suggested that board meetings included only routine items and that there was no discussion or questioning of items included on the agenda. A distinguishing feature of these boards was that they had a role to play (in terms of control, service, and/or strategy). The control role was evident in the boards’ monitoring of the financial situation and their implementation of strategies and plans. The service role was apparent in the CEOs’ assertions that their boards were of value to them in managing their firms. Finally, with respect to a strategic role, a clear difference emerged between the first two clusters—with the boards in the ‘professional’ cluster contributing ‘vision’ to a greater extent than those in the ‘paperboard’ cluster.
In the ‘management lead’ cluster, the working style of the boards was somewhat more structured than in the ‘paperboard’ cluster. Boards met officially approximately four times a year; in addition, there were many informal meetings among members of the management team. The majority of board meetings had a meeting agenda that was distributed beforehand, and minutes were usually kept. However, as can be seen from Table 3, the results with respect to the other two variables measuring working style (‘amount of discussion’ and ‘routine items’) were ambiguous and did not indicate that the boards were particularly effective or ineffective. Nevertheless, it is clear that the boards in this cluster had a strong service role; indeed, the CEOs in this cluster were more likely than CEOs in other clusters to see their boards as important ‘sparring partners’. This could be explained by the fact that the CEOs in the ‘management lead’ cluster were more likely to be working on a daily basis with the members of the board (who also constituted the management team). In contrast to the ‘paperboard’ cluster and the ‘professional’ cluster, the ‘management lead’ cluster was more likely to have the CEO and board working together as an integrated team. The boards in this ‘management lead’ cluster also had a strategic role; the board was more likely to contribute in terms of vision and goals than was the case in the ‘paperboard’ cluster (albeit less than was the case in the ‘professional’ cluster).

4.4. Board Effectiveness and Firms’ Characteristics

The statistical analyses showed that the various clusters differed with regard to major developments in the preceding three years—such as internationalisation, large investments, or significant increases in the number of employees. In the ‘professional’ cluster, 75% of the firms had experienced such major developments, whereas only 7% of the firms in the ‘paperboard’ cluster and 40% in the ‘management lead’ cluster had experienced such developments. Thus, the results indicate that there is a relationship between firm activeness and board effectiveness. On one hand, this could be seen as a tendency that a general ambition and willingness to actively develop the firm also includes a more open attitude towards the board of directors. On
the other hand, stable firms might not perceive the same need to have an effective board as firms characterised by change and development.

According to the statistical analyses, the three clusters also differed with respect to annual financial turnover. The highest turnover was found among firms in the ‘professional’ cluster and the lowest among the firms in the ‘paperboard’ cluster. However, no differences were found with regard to age of the firms, number of employees, or industry.

5. Conclusions, Limitations and Future Research

5.1. Major Conclusions

The purpose of the present study was to investigate boards of directors in small firms and more specifically to explore the link between board effectiveness and the composition, roles and working styles of the boards. There have been several calls for research on board behaviour investigating the working processes of boards (Forbes and Milliken 1999; Huse 2000; Uhlaner et al. 2007). Moreover, research drawing on detailed data about individual board members and board roles is scarce (Huse 2000). The main contributions of this study are hence that it explores how boards in small firms actually function and gives a detailed account of their composition and roles.

The study has identified three groups of small firms with respect to board effectiveness—from ‘professional boards’ to obvious ‘paperboards’, as well as a third cluster of ‘management lead’ boards. This range of board effectiveness indicates that it is inappropriate to presume that boards of directors are universally perceived as ‘resources’ in small firms (as ‘resource-dependence’ theory might suggest); conversely, it is inappropriate to presume that boards of directors are universally perceived as a ‘necessary evil’ in such small firms (as the theory of ‘managerial hegemony’ might suggest). Moreover, this study has demonstrated, that effective boards can also be found in the ‘management lead’ cluster. Taken together, for a board to be considered ‘effective’, it is not necessary for all three roles (‘control’, ‘strategic’, and ‘service’) to be equally prominent, nor is it necessary to have a high proportion of outsiders or a formal
working style; rather, a board can demonstrate variations with regard to these different dimensions and still be considered ‘effective’ (cf. Uhlaner et al. 2007).

It is maintained within research on boards in small firms that the control role is not prominent (Forbes and Milliken 1999; Van den Heuvel et al. 2006; Zahra and Pearce 1989). However, the findings demonstrate that some aspects of the control role are perceived as important especially in the ‘professional’ cluster, but also in the ‘management lead’ cluster. Thus, it cannot be assumed that ‘professional’ boards fully coincide with the presumptions of the resource dependency theory, which only emphasises the strategic and service roles. However, even though the control role was evident, the control of CEOs is not emphasized in any of the clusters, which in extant research is considered a vital part of the control role (for example, Zahra and Pearce 1989). This can be explained by the fact that the proportion of independent board members is positively related to the control role in small firms (cf. Gabrielsson and Winlund 2000). In this study the number of independent members is small.

The study has also revealed that a substantial proportion of the members of boards in small firms consist of representatives from the management team; that is, in practice, the management team and the board are substantially intertwined, even though they are formally constituted as separate bodies. The management team may even substitute the board (cf. Uhlander et al. 2007). This supports the findings of Brunninge et al. (2007), who concluded that the roles of the board and the management team are not clear cut and separate in small firms. The present study shows that most of the CEOs are content with the prevailing arrangements because they consider that the management team has the knowledge and experience to handle the tasks traditionally assigned to the board. Nevertheless, the study also identified CEOs who perceive a need to develop the board in terms of role, composition and working style.

5.2. Limitations and Further Research

Although the present study has found that there is a link between board effectiveness and the role, composition and working style of boards of small firms, other potentially influential
factors are also worthy of investigation; for example, the personal characteristics of the individuals involved, generational factors in family firms, and the situational circumstances of various firms could also be taken into account. Even if an effective board is strived for, other factors (such as the inability of the CEO to develop an effective board in practice, or the CEO’s inability to implement board-effectivating measures) might cause the board to maintain a relatively passive role. Conversely, in a firm where a paperboard would be desired, various situational factors to introduce an effective working style on the board might occur, for example, if a venture capitalist demanded such changes. The effect of generational factors (see Bammens et al. 2008) on the results of our study would also have been interesting to investigate. These personal, generational, and situational factors are worthy of further research.

In addition, the intertwining of the management team and the board (as identified in the ‘management lead’ cluster) deserves further attention. In the present sample of small firms, this cluster was the largest of the three identified clusters. In most of the extant literature, management teams and boards are treated as separate entities; the lack of research on the embeddedness of management within boards is hence worthy of further investigation.
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