BOARD DIVERSITY AND GENDER QUOTAS

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Synonyms

Board heterogeneity

Definition

Board diversity refers to the "board composition and the varied combination of attributes, characteristics and expertise contributed by individual board members in relation to board process and decision making" (van der Walt andIngley 2003 p. 219). Gender is the most relevant feature that may drive board diversity. As a matter of fact, different countries are introducing regulations promoting the appointment of female directors to boards with the purpose of fighting gender inequality in top corporate positions.

Introduction

Board of directors' diversity is a broad concept that refers to the "board composition and the varied combination of attributes, characteristics and expertise contributed by individual board members in relation to board process and decision making" (van der Walt andIngley 2003 p. 219). This definition emphasizes two relevant aspects of board diversity: (i) the antecedents of diversity and (ii) its effect (Rao and Tilt 2016). Board diversity is a multidimensional concept driven by distinct individual director attributes; some are observable (e.g. gender, age, race, or nationality) while others are less apparent (e.g. experience, functional background or education) (Kang et al. 2007, Pelled 2006). Board diversity may affect the operation and dynamics of boards, thereby influencing performance in monitoring and advisory tasks. In line with resource dependence theory (Pfeffer and Salancik 1978), board diversity represents a source for creativity, innovation, and original solutions to problems (Carter et al. 2003,Huse et al. 2009). Directors of diverse backgrounds, knowledge, and skills might contribute to the strategic advisory role of boards by fostering different perspectives (Harjoto et al. 2015, Shaukat et al. 2016). However, it is important to balance the presence of diversity in the board given that too much heterogeneity among directors could lead to conflict and may result in the obstruction of consensus and deterioration of the board decision-making process (Lau and Murninghan 1998, Harjoto et al. 2015).

By means of its influence on board tasks, board diversity is an important determinant of firm performance in both financial and corporate social responsibility (Rao and Tilt 2016). Boards of directors are an important determinant of CSR practices given that one of their duties is to provide management with strategic advice (Jamali et al. 2008). By broadening the perspectives and backgrounds in the boardroom, diversity fosters the sensitivity of the board towards all stakeholders, not just towards shareholders (Harjoto et al. 2015, Rao and Tilt 2016).

Nowadays, the presence of female directors is the attribute most subject to attention among the different demographic characteristics that could lead to diversity. Gender inequality in top corporate positions is a global issue. This issue is particularly relevant when analyzing board of directors because women are significantly underrepresented as compared to their male peers (Terjesen et al. 2015). Female directors are more likely to be on boards in countries with more females in top management, a lower gender pay gap and a lower presence of women in political positions (Terjesen and Singh 2008). In addition, the representation of female directors is greater at family firms, where they are usually appointed for simply being part of the family (Terjesen et al. 2015).

The overall smaller presence of women on boards is driven by a gender-stereotype effect in the board recruitment process. Women consistently face greater difficulties than men in achieving top level positions due to a "glass ceiling" effect. This term refers to invisible barriers impeding the promotion of women within organizations. These barriers are linked to an unjustified social belief claiming that women lack the adequate human capital in terms of skills, experience and background to properly undertake upper-echelon positions (Powell 1999, Lyness and Heilman 2006). The similarity-attraction paradigm (Byrne 1971) and homosocial reproduction theory (Daily and Dalton 1995) also suggest that individuals are more comfortable working with people akin to them (Byrne 1971). Thus, CEOs and current directors, mostly men, are more likely to support the appointment of new male directors (Terjesen et al. 2009). Women are required to possess greater skills and abilities to attain the same board position. The lack of transparency in director recruitment and appointment has contributed to maintaining biased and inadequate selection procedures.

Gender inequality is undesirable because it represents an ethical and moral problem; it restricts the access of women to the boardroom. Furthermore, it creates problems for firm effectiveness because they do not exploit talent from the pool of suitable director/management candidates (Terjesen et al. 2015, Terjesen and Sealy 2016). Thus we may observe a growing social and governmental demand to increase female participation in top-level positions, especially on boards of directors. Some countries, especially in Europe, have responded to this demand by proposing several instruments to promote/encourage the appointment of female directors.

Gender diversity has become an important topic of debate subject to growing public attention. This relevance has given way to a significant line of research that studies the antecedents, motivations and consequences of the presence of women on boards and gender quotas. The papers of Terjesen and coauthors on these issues, quoted throughout the text, help to understand these phenomena.

Instruments to promote the presence of women on boards

Two types of instruments are currently being used to increase the representation of women on boards of directors. Some governments are advocating soft law regulation by proposing voluntary mechanisms while others have decided to establish hard law regulation through mandatory mechanisms (Terjesen et al. 2015). The most common measure among the voluntary instruments is the inclusion of recommendations on board gender equality in national corporate governance codes (e.g. Australia, Austria, Denmark, Germany, Ireland, Luxembourg, Malawi, Malaysia, The Netherlands, Nigeria, Poland, South Africa, Sweden, United Kingdom and the United States) (Terjesen et al. 2015). Some of these codes set a voluntary target for the proportion of female board members. In contrast to this approach, others simply highlight the importance of fighting gender inequality and the need to appoint female directors. The recommendations usually follow the "comply or explain" principle: firms must indicate whether they comply with the gender recommendation and explain why if they fail to do so. In addition to corporate governance code recommendations, other voluntary mechanisms are available, e.g. proposed training and mentoring programs, awards for gender-balanced companies, or the creation of databases on qualified women for board positions (European Union2013).

Regarding the legal mechanisms, some countries set mandatory quotas so that women must represent a specific proportion of board members. Companies are required to meet the quota and may face sanctions if they refuse to do so. The specific requirements of the quotas vary from one country to another. For instance, targeted firms could be state-owned, public, or both. The required proportion of women also differs significantly. It goes from the presence of at least 1 female director in India and United Arab Emirates to 50% in Quebec (Canada) and Austria. The timetable for the quota implementation and the sanctions for firms also vary. In Norway, penalties are strict, even leading to firms being delisted or dissolved. By contrast, Spain prescribes no sanctions. The Spanish government tries to incentivize compliance with the quota by providing benefits to complying firms. In Italy, penalties become stricter the longer the company fails to comply; they may even result in the annulment of the board of directors.

European continental countries are more likely to establish board gender quotas. According to Terjesen et al. (2015), countries with quotas are usually characterized by three institutional factors. Quotas are more likely in countries with more policy welfare provisions, a left-party government, and a history/record of numerous initiatives fostering gender equality at the political and corporate levels.

The European Union advocates the establishment of gender quotas on boards of directors. The European Commission submitted a proposal for a directive on board gender equality in 2012. The proposed directive states that the under-represented sex should account for 40% of non-executive directors at listed companies. Firms may also comply with the directive if the under-represented sex represents at least one third of all board members. The deadline for attaining this target is 2020. The proposal considers sanctions, such as administrative fines or the annulment of the appointment of directors, if companies fail to achieve the 40% goal/target. Although the proposal is currently under study, the European Parliament has already claimed its support for the directive, but some member countries are against establishing binding quotas.

Motivations for establishing board gender quotas

Proponents base their justification for establishing board gender quotas on two types of arguments: (i) a quest for justice and (ii) a potential positive effect on company performance. The first type of reasoning, justice, is grounded on the access of men and women alike to the same positions. The Article 2 of the Universal Declaration of Human Rights states that no distinction should be made among human beings based on sex. However, as above-mentioned, the presence of significant differences between genders in access to jobs is owed to the fact that women face stronger barriers to access top level decision-making position in firms than do men (Terjesen et al. 2009). As a minority group, women require higher qualifications to overcome discrimination stereotypes for a directorship (Hillman et al.2002). Board gender quotas help to achieve equality by promoting the under-represented sex to make an equitable distribution of top-level corporate positions. Increasing female representation on boards contributes to "building more inclusive and fairer business institutions that better reflect their present generation of stakeholders" (Terjesen et al. 2009 p. 320).

The second type of reasoning argues that the presence of women on boards enhances the performance of firms (Terjesen and Sealy 2016). By considering women in selection procedures and appointing them to board, firms effectively utilize the pool of human capital and hire the most talented individuals. If this is properly done, the presence of women increases the diversity of skills and abilities in the boardroom and contributes to the board decision-making process. Women are different to men in terms of backgrounds, experience, and personalities (Huse 2008, Terjesen et al. 2009). Furthermore, female directors also improve knowledge because they usually hold higher academic qualifications and broader international experience than their male counterparts (Singh et al. 2008). The diverse set of individual member attributes and characteristics fosters innovation, creativity, and the problem-solving capacity of the board as a whole. These enhancements to the board's decision-making process ultimately lead to improved financial performance. Female presence is also likely to improve CSR performance because women are more sensitive to all of the stakeholders' concerns (Terjesen et al. 2009). Nonetheless, female directors may feel constrained and may be reluctant to express their opinions (Terjesen et al. 2009). Thus, the positive effects provided by women may not take place unless a critical mass of them are represented on the board (Konrad et al. 2008). Establishing gender quotas helps to achieve this critical mass of women and thereby leverage this positive impact.

Finally, board gender quotas are expected to have a spillover effect and increase female presence at all company levels as well as in the economy. They may also help to reduce the gender-pay gap. What is more, female directors may motivate other women to access management jobs (Bilimoria and Wheeler 2000).

Are quotas achieving their expected goals?

Quotas are useful instruments for increasing the number of females, especially as compared to non-binding measures like recommendations on corporate governance codes directors (Walby and Armstrong 2012). However, the presence of women on boards of directors is still low (Terjesen et al. 2015). Despite the improvements they have driven, quotas fall short of being effective to adequately increase female board representation. The severity of the non-compliance sanctions established by the country issuing the quota seems to partly determin the achievement of the target For instance, sanctions in Norway are hard, and they could eventually lead to the dissolution of the company. Thus, the majority of the Norwegian companies affected by quotas achieved the 40% target. By contrast, many Spanish firms do not meet the same 40% threshold suggested by their national quota. Spain follows an incentive approach with no particular sanctions for companies failing to meet the quota.

Whether or not the representation target is met, several issues question the suitability of legally imposing board gender quotas. Although gender inequality on boardrooms is undesirable, quotas may raise ethical tensions because they try to "prevent discrimination by utilizing discrimination" (Terjesenand Sealy 2016 p. 33). The establishment of a quota might bias the selection procedure for new directors as firms may have to hire women to meet the quota regardless of their qualifications (Terjesen et al. 2015). In so doing, quotas reduce the freedom of companies and their owners to select the most suitable individual. As a consequence, newly appointed women could feel their nomination is less legitimate because they may have been hired for firm compliance rather than for their actual merits , (Sealy 2010). Nonetheless, after the quota is met, women consider they really improve the performance of the board because they are more qualified than former male directors (Terjesen and Sealy 2016).

Another problem relates to the scope of the quota. The change led by quotas is quite limited because, as Terjesen et al. (2015) noted, most of these quotas only affect listed and state-owned firms, while most companies are private. Additionally, quotas fail to increase the pool of women candidates when analyzing new board appointments because same women are actually appointed on different boards. This group of women is known as the "golden skirts" (Huse 2011).

Finally, it is noteworthy to point out that quotas could also create organizational problems, particularly for multinational companies. They could create market barriers because the voluntary or mandatory nature of female board representation may vary among countries in function of the targeted firms and fixed proportion (Walby and Armstrong 2012).

To conclude, even though quotas help to increase the presence of women on boards, they still present some inefficiencies making their suitability questionable. They should therefore be combined with other mechanisms that contribute to promoting female representation. To this respect it seems crucial to establish instruments to fight/break the barriers impeding/hindering the access of women to top level positions in the first place. Gender equality can only be effectively achieved by diminishing the cultural and environmental factors obstructing the absence of discrimination in the job market. can.

Cross-references

→ See **Board capital**

→ See **Diversity of boards**

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