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978-0-521-60634-9 - Boards, Governance and Value Creation: The Human Side of Corporate Governance

Morten Huse

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Boards, Governance and Value Creation

What is the role of boards in corporate governance? How should they be used and developed in order to maximise value creation? This book looks at boards in a variety of countries and contexts, from small firms to large corporations. It explores the working style of boards and how they can best achieve their task expectations. Board effectiveness and value creation are shown to be the results of interactions between owners, managers, board members and other actors. Board behaviour is thus seen to be a result of strategising, norms, board leadership, and the decision-making culture within the boardroom. Combining value creation, behavioural and ethical approaches to the study of boards, this work offers a systematic framework that will be of value to reflective practitioners, graduate students and researchers in the fields of business ethics, strategic management and corporate governance.

Morten Huse is Professor of Innovation and Economic Organisation at the Norwegian School of Management and Visiting Long-Term Research Professor in the Department of Strategy at Bocconi University, Milan.

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‘This is an extraordinarily insightful book on an important and timely topic: what boards do and how they add value in different organizational settings. Cognizant of the legal and political debates on corporate governance, Morten Huse pays special attention to board dynamics and how they influence the processes directors follow in making their decisions, bringing a fresh perspective on boards as a key instrument of governance. Huse’s attention to smaller and privately held companies is an important contribution, as is his discussion of effective ways to revitalize boards. The artful analysis of the various systems of governance worldwide is another contribution. This is an important book with a clear and an important message. Huse reaches the top of his craft, eloquently enriching the debate on the importance and future of boards. This book is a must-read for scholars, managers and public policy-makers.’ (Shaker A. Zahra, *Professor and Robert E. Buuck Chair in Entrepreneurship, Co-Director, Center for Entrepreneurial Studies, and Co-Director, Center for Integrative Leadership, University of Minnesota, Minneapolis*)

‘At last, a book about the human side of corporate governance. This is a refreshing and intellectually invigorating read for anyone who is serious about understanding the vital role of boards and governance in value creation.’ (Andrew Crane, *George R. Gardiner Professor of Business Ethics, Schulich School of Business, York University, Toronto*)

‘Morten Huse presents us with a major work in the area of corporate governance, which is the result of not only an in-depth research programme conducted by one of the top-class scholars in the field, but also of twenty years’ experience studying boards throughout Europe. Huse provides us with a unique synthesis. This work reflects the kind of wisdom that is acquired only through years of interaction with directors on a both professional and personal level. There is no doubt that it will become a reference work for researchers as well as for practitioners who are involved on a day-to-day basis with boards and questions of governance.’ (Pierre-Yves Gomez, *Professor in Strategic Management, Director, Institut Français de Gouvernement des Entreprises, EM Lyon Business School*)

‘Prof. Huse’s book is based on two key premises, that the main task of a board of directors is to create value for the firm, and that to understand this value creation process one needs to look inside boards and understand how the team of directors works. Both premises are true and important. Thanks to the serious research he and his colleagues have carried out in the past twenty years, this book is a major contribution to our understanding of the realities of the fundamental task of corporate governance. A book every director should read!’ (Joan E. Ricart, *President, European Academy of Management and Strategic Management Society, and Carl Schröder Chair of Strategic Management, IESE Business School, University of Navarra, Barcelona*)

‘This book successfully combines the value creation and the behavioural and ethical approaches to the study of boards, offering a systemic framework which contributes both to the practitioner and the academic debate. I’m especially pleased to see that the subject of corporate governance is deployed with reference to all classes of firms and to different stages of their life, whereas most literature is still concentrated on large listed companies. The book suggests a wide range of different views and interpretations of the roles of boards and governance in our society.’ (Giuseppe Airoldi, *Professor of Business Administration, Institute of Strategic Management, Bocconi University, Milan*)

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Boards, Governance and Value Creation

The Human Side of Corporate
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and Bocconi University, Milan*



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Preface

A past president of a large multinational corporation recently confronted me with the view that corporate leaders and board members have not learnt anything from research into corporate governance. This observation has at least two aspects to it. The first is that corporate governance research needs to be relevant and actionable. The second is that research-based findings must be communicated. Through this book my aim is to communicate actionable research and knowledge about boards and governance.

My objective is to stimulate thinking, rather than to produce a handbook that purports to present definitive answers to various questions. This is a research-based book that, it is hoped, will help the reader reflect on and gain a deeper understanding of boards and governance. But it is also a book that communicates actionable knowledge with regard to boards of directors. Thoughtful readers are the target group; these may be board members, potential board members, business school students, researchers, or others who may have an interest in boards. The book has an ambitious objective: it is written in a management tradition with an emphasis on strategic decision-making, organisation theory and organisational behaviour. Value creation, including entrepreneurship and corporate social responsibility issues, are used to frame the presentation.

Boards of directors in different countries and contexts

The tasks facing boards of directors have received considerable attention of late, and in a range of countries. The attention has to a considerable extent focused on large corporations following the corporate governance debate, but there is also an increasing emphasis on boards in small and medium-sized enterprises (SMEs), including family businesses. Few business topics seem to be so urgent to explore and understand today as boards and governance.

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The focus of this book is boards and some aspects of governance or corporate governance. When I say ‘the board’ I mean the board of directors – the organisational body that, in most countries, is usually expected to hire, fire and compensate the chief executive officer (CEO) or the top manager, to set objectives for the firm and to ask discerning questions. However, the formal setting may vary between nations. The book has, therefore, been written so as to meet the differing needs of different countries and different firm sizes. Examples are taken from various countries and from firms of various sizes.

Corporate governance systems vary between countries. A delegated system exists in most places in continental Europe, whereas there are no formal delegation requirements in the United States or the United Kingdom. In this book I address both delegated and non-delegated systems, and I put forward the proposition that, in trying to understand value creation and the human side of governance, the similarities may be greater than the differences. When I write about boards I am referring to the supervisory boards to be found in the German and other two-tier board systems. When I write about the CEO and management, in the two-tier board system it will often refer to the executive boards.

Frequently I talk about firms. However, many of the concepts and relationships presented are more general and may also be applied to boards of voluntary or public organisations, or even project teams. Even though I do not always specifically address boards in SMEs, the book is written in the clear understanding that most firms fall into this category. The book is premised on a corporate governance setting, but boards and governance are also important for activities and enterprises other than large corporations.

Value creation and the human side of corporate governance

The title of this book underlines the emphasis on value creation. The value creation concept is introduced for three reasons. First, it is written in a tradition that sees organisations as tools to create value. This book is intended to be a contribution to board effectiveness and accountability. Second, I see value creation as a broad concept, in which different stakeholders may all make a variety of contributions to the value creation concept. Third, the value creation concept focuses on the board’s task in creating value throughout the whole value chain and not just in the value distribution phase.

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This book has an open system approach to understanding actual board behaviour and the human side of corporate governance. Understanding actual board behaviour means understanding the underlying processes that go on behind boards' public actions and statements. It goes beyond assumptions about what boards are doing, and it explores boards' working style and how closely in practice boards meet their task expectations. An open system approach also means that we may go outside the boardroom, and even the board members, in order to understand how the boards' decision-making is influenced and formed.

The evolution of the book

This book has been in gestation for more than fifteen years. In 1989 I started teaching my first Master of Science class about boards and governance in Norway, at Bodø Graduate School of Business. I had then just started my research agenda on boards of directors. Since then between twenty and thirty research projects on boards and governance have followed, and the results of these projects have been presented in various articles and publications. This book presents the accumulated findings and conclusions resulting from this research, teaching and consulting. Many sections of this book are based on, and make use of, work that was developed with colleagues and published in various articles. I am very grateful for the contributions of these colleagues. The notes found at the end of this volume indicate the articles and the colleagues that various sections draw on. Here I would particularly like to mention Huse and Rindova (2001) in chapter 2, Gabrielsson and Huse (2005) in chapter 4, Van Ees, Gabrielsson and Huse (unpublished) in chapter 6, Huse and Eide (1996) in chapter 6, Huse, Minichilli and Schønning (2005) in chapter 8 and Huse, Minichilli and Gabrielsson (forthcoming) in chapter 10.

The first full textbook based on this teaching and research was published by the Nordland Research Institute, Bodø, in 1993 (in Norwegian). The title then was (in English) *Aunt, Barbarian or Clan: About Boards of Directors*. The Norwegian publisher Fagbokforlaget, based in Bergen, decided to publish a revised version of this book in 1995. A new version, incorporating major revisions, was published in 2003. The title was then changed to *The Board: Aunt, Barbarian or Clan?* Both versions from Fagbokforlaget are in Norwegian.

Boards, Governance and Value Creation: The Human Side of Corporate Governance is based on new and different concepts, and was

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conceived with a non-Scandinavian audience in mind. The core ideas and the basic framework of the book have been developed and refined in published articles¹ and conference presentations, and through MBA teaching and research seminars at universities in Norway, Sweden, Finland, the Netherlands, France, Switzerland, Italy, Ireland and the United States.

Research projects

This book is not the result of a single research project but, rather, has evolved through experiences gained from many projects. Several of my own projects will be referred to throughout the book, and when referring to them I use certain labels or nicknames. These are listed below.

- The ‘distanced closeness’ study,² which was my doctoral dissertation. It had a deductive-theory-driven empirical design, and in it I tried to solve the paradox of simultaneous independence and interdependence in board–management relationships.
- The ‘bankruptcy’ study³ had a matched-pair design. I studied board compositions in small firms that had filed for bankruptcy, and for each of the forty-four bankrupt firms a twin firm was found. A time series approach was used and the findings were supplemented with qualitative data.
- The ‘one of the lads’ study⁴ was designed to explore interactions inside and outside the boardroom. Participant observation methodology was used while I was the board chairperson in three small firms in different life cycle phases. Various illustrations from this study are presented in chapters 5 and 6.
- The ‘U’n’I’ study⁵ was a reconstructive case study based on newspaper articles, reports and interviews with actors and informants. The objective of the study was to explore the power bases and techniques that the CEO in a large financial corporation uses to circumvent the corporate governance mechanisms. An extract of this study is presented in chapter 6.
- The ‘board life story’ study⁶ was based on collecting and analysing the life stories of women corporate directors. The objective was to explore the experiences of women directors and to get a gendered perspective on boards of directors. Illustrations from this study are presented in chapters 6, 7 and 8.

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- The ‘fly on the wall’ study⁷ was based on observations over a period of one year in the boardroom of the TINE Group. The objective was to explore boardroom dynamics. Interviews with all the board members and the top management team (TMT) were also conducted. Extracts from this study are presented in chapter 8.
- The ‘value-creating board’ programme⁸ consisted of large-scale data collections in various surveys. The surveys took place in Norway and various other European countries. The survey instrument followed the framework adopted in this book. In Norway the responses were collected from CEOs, board chairs and other board members. The responses were collected at two points in time. Results from this study are presented in chapters 9 and 10.

Other studies have also been conducted, including the subsidiary board study,⁹ the environmental reporting studies,¹⁰ the venture capitalist studies¹¹ and the innovation studies.¹² When referring to the various projects I sometimes use the first person singular, ‘I’, and sometimes the plural, ‘we’. Generally, ‘we’ is used when the contribution was made in conjunction with colleagues.

Framework and outline

In this book I use a framework for the understanding of behavioural perspectives on boards so as to guide the reader. The framework is presented in chapter 1, and each of the subsequent chapters is devoted to one of the main elements in the framework. Theoretical and practical issues are presented in each chapter. Chapters 4 to 9 include in-depth case studies. These case studies employ and summarise concepts from the preceding presentations, and they are used to investigate certain topics more deeply.

Sometimes the first person plural form, ‘we’, is used, which denotes that I am including the reader in the presentation. However, sometimes the singular pronoun ‘I’ is the most natural – in particular when it refers to my own private experience. Books, chapters, sections or tables are considered to be passive objects that cannot say, indicate, present or show anything by themselves; nevertheless, in order to simplify long and difficult sentence constructions, I let these objects constitute the subject of many sentences.

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*Preface***Acknowledgements**

There are many people who have supported me in the writing of this book, and they have contributed in various ways. First I would like to express my thanks to my family, who have seen me at work on this book for years; the manuscript has accompanied me all the time! Next I thank Jonas Gabrielsson, my former student, colleague and friend. His thinking has continually stimulated me in my writing, and he has made useful comments not only during the preparatory period but also, in more detail, on late drafts of my manuscript. I would also like to thank Shaker Zahra, for a long-standing friendship and many lengthy and interesting discussions, which led to this manuscript. Then I would like to put on record my gratitude to all those whom I have worked with at the Norwegian School of Management on the 'value-creating board' project. They include Cathrine Hansen, Ping Wenstøp, Margrethe Schøning, Edle Gjøn, Lise Haalien, Jon Erik Svendsen, Elbjørg Gui Standal, Jon Erland Lervik, Ingjerd Jevnaker and Thomas Sellevold. Thanks must also go to the Norwegian Research Council and other sponsors of the project.

In addition, I would like to acknowledge my colleagues at Bocconi University, participants at the three Norefjell workshops on behavioural perspectives on board research, and the colleagues who are carrying out comparable research in other places. I thank all those who have read my manuscripts at various stages along the way, mentioning in particular Hans van Ees, Anita van Gils, Mattias Nordqvist and Alessandro Zattoni, all of whom have given me comments on the final draft. I would also like to mention Inger Marie Hagen, Sabina Tacheva, Luca Gnan, Alessandro Minichilli and Amedeo Pugliese for valuable discussions in the latter stages of the manuscript's preparation, and Anna Grandori, Sven Collin and Giuseppe Airoidi for important insights in the process.

Thanks must also go to co-authors and colleagues on various earlier manuscripts that I am using in this book. They include Dorthe Eide, Halvard Halvorsen, Anne Grethe Solberg, Diana Bilimoria, Bengt Johannisson and Violina Rindova. I am grateful to Tom Keogan for making the English-language corrections to the manuscript and to Bård Hansen for compiling the references. Thanks also to Katy Plowright, Paula Parish and other editors at Cambridge University Press, and also to my Norwegian publisher Fagbokforlaget.

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