Gender quotas and the financial crisis

Boardroom,Editorial,Quotas

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New research on publicly quoted companies sheds a remarkable light on how two mechanisms at work in the boardroom reinforce each other: the glass ceiling and challenge from independent directors on strategy. The much-discussed idea that all would have been different if Lehman Brothers had been 'Lehman Sisters" is now not a rhetorical jibe but a credible argument.

Michael McDonald and James Westphal surveyed all first-time director appointments at the 2,000 largest publicly quoted American companies over an eight-year period, and tracked what happened over the subsequent two years.

Of the sample, more than 1,000 were first-time directors. In more than 80 per cent of cases the researchers obtained cross-checking perspectives about individuals and events from two or more experienced directors on the same boards. They used extensive checks to screen out misleading statistical effects.

Some of their results do not surprise. Women and ethnic minority first-time directors are less likely to receive mentoring on how to act in the boardroom than white males, for example.

But the study goes on to demonstrate the importance of mentoring by showing that this lack makes individuals less likely to secure additional board appointments. Women and ethnic minorities made up 28 per cent and 22 per cent respectively of those individuals who held one board seat, but the percentages were much lower — 8 and 5 per cent — among those holding more than one seat. Securing additional appointments not only means more clout in more places, it also means having more clout in any one place, because the individual is recognised as part of a wider directorship elite.

Mentoring matters, especially in the first six months of joining a board, because first impressions last. If a first-timer violates unwritten boardroom norms early on (or is too timid to make an impact for fear of violating them), there will be a continuing effect on other board members' assessment of their calibre.

The shocker in McDonald and Westphal's work is that there is an unwritten boardroom norm, which a newcomer might find impossible to learn without mentoring, and which is central to the role of boards in averting the next financial crisis, regarding independent challenge of strategy.

In the study, 95 per cent of experienced directors agreed that their normal role on strategic matters was to advise the chief executive, rather than to exercise control; 93 per cent would normally only raise concerns about strategy in a boardroom if the chief executive had given prior permission. One experienced director commented in the report: "So as a good director I would clear the [strategic] issue with the CEO in advance. If he says it's a go, I mention it in the meeting... if he doesn't think it's worth discussing, I don't raise it."

In the absence of mentoring, first-timers will observe some strategic challenge going on but not be aware that it is taking place by permission. The study confirms that "directors are unlikely to reveal in a formal board meeting that they cleared an issue with the CEO in advance, as they (and a firm's CEO) will tend to prefer that this fact not be recorded in meeting minutes".

In effect there is a pantomimic dimension to strategic challenge which double-glazes the glass ceiling and puts into question nearly every post mortem examination of the financial crisis.

One transatlantic difference is that commonly in the US, the chief executive is also chairman of the board, unlike the separation of executive and non-executive powers in the UK. Women currently hold 17.3 per cent of FTSE 100 board seats in the UK, meaning that a 45 per cent increase in two years will be necessary if the goal of 25 per cent in 2015, set by Lord Davies's report, is to be achieved. At that point, in a UK general election year, inadequate progress could put gender quotas back on the agenda. This research adds to the case for such a quota. The authors note that having women on boards is associated with greater board independence from management, and greater board engagement in strategic decision-making.

Do we want to mentor new women directors into a flawed model, or would we rather have them in the front line of asking unwanted as well as wanted strategic questions?

If the latter, then a gender quota (perhaps for an initial period of 10 years) would provide a safety net for them to make a viable career and show us a different way of "doing boards". Of course there would be costs, but possibly less than another crisis.

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