

Board Tasks in Small Firms: The Importance of Motivation and Evaluations

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Abstract

The attention to board of directors in small firms is increasing. Traditionally they have been considered to be passive and labeled paper boards or aunt boards. However, boards in small firms are now undergoing major changes. In this paper we test hypotheses of what makes boards active and allows them to contribute to value creation. Activity is seen in relation to board task involvement. Predictions based on agency theory, resource dependence theory and the resource based view of the firm are used to explore board task involvement. In a sample of 347 small firms we got strong support for hypotheses highlighting the use of the knowledge of the board members and various board maintenance tools, such as regular board evaluations, to increase board task involvement. Various contextual variables were included as control variables, but few were significantly related to board task involvement. Actionable advice to boards in small firms is provided.

Key words: board of directors, small firms, board task involvement

1. Boards in Small Firms: What Makes them Active?

Our purpose with this paper is to explore what makes boards in small firms active. Research on boards and governance has increased during the recent years, but we still know relatively little about governance and boards in small firms (Fiegeneger, 2005; Huse, 2000). It is widely acknowledged that small firms have

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certain characteristics that make them a special case of governance in need of particular attention (Cowling, 2003; Huse, 2000). The typical overlap of governance structures (Brunninge et al., 2006) and the lack of functional managerial competence (Cowling, 2003) are only two examples of such characteristics.

Some research exists on the roles that boards can play in small firms (Corbetta & Salvato, 2004; Dyer, 1986; Fiegner, 2005). However, boards in these firms are often considered to be legal bodies with limited importance. Such boards are usually referred to as 'paper boards' (Dyer, 1986) or 'aunt boards' (Huse, 2003), since they are typically composed of persons close to the owner-manager that are willing to lend their name to meet legal requirements.

Small firms are like the larger firms experiencing increasing pressures to activate their boards for value creation (Corbetta & Salvato, 2004; Nordqvist & Melin, 2002). The lack of research addressing what actually makes boards in small firms active and contributing to value creation is therefore a significant limitation of the current literature. We especially know little about how factors beyond the traditional contextual variables, CEO attributes and board composition (Daily, Dalton & Cannella, 2003; Finkelstein & Mooney, 2003; Forbes & Milliken, 1999) affect board activity in small firms. Few studies have for instance explored the impact that the use of the board members' knowledge and skills (Forbes & Milliken, 1999; Huse, 2000; Zona & Zattoni, 2007), their intrinsic motivation (Borch & Huse, 1993; Hermalin & Weisbach, 1988, 1991), and the board development tools like board evaluation (Gabrielsson & Winlund, 2000; Minichilli, Gabrielsson and Huse, 2007) have on board activity.

Board activity has in earlier studies been defined as the number of outside board members and the number of board meetings. However, in this paper we argue that these proxies do not fully grasp board activity and in particular board value creating activities. We therefore mainly use an alternative construct - board task involvement - as a measure of board activity. Various board tasks have theoretically been argued to have value creating contributions (Huse, 2005; Johnson, Daily & Ellstrand, 1996; Minichilli, Zattoni & Zona, forthcoming) and board task involvement refers to the extent to which the board as a group is involved in these tasks (Forbes & Milliken, 1999; Huse, 2005; Pearce & Zahra, 1991). Task involvement may directly be related to value creation (Huse, 2005) and various theoretical perspectives emphasize different board tasks such as control, service and strategy (Zahra & Pearce, 1989). Arguments from agency theory, resource dependence theory and the resource based view of the firm highlight the importance of different board tasks. In this study we test in a sample of small firms how predictions from these theories explain board task involvement.

Both empirical and theoretical contributions are made. First, we explore how traditional predictors explain board task involvement in small firms. Research on boards has mostly been about large and publicly traded corporations, and the most used predicting variables, 'the usual suspects' (Finkelstein & Mooney, 2003), have been the number of board members, CEO duality, outsider ratio and the shareholding of the board members. Second, we go beyond these variables and

explore the importance of the intrinsic motivation of board members (Fama & Jensen, 1983; Hermalin & Weisbach, 1988; 1991; 1998). The basic argument is that it is not enough for board members to have knowledge and skills, but they also need to use them (Forbes & Milliken, 1999). Third, we explore how some board structures recommended in the current practitioner oriented literature affect board activity. The introduction of regular board evaluations (Behan, 2004; Huse, Minichilli & Schoning, 2005; Minichilli et al., 2007) and the allocation of more time during board meetings (Demb & Neubauer, 1992) are two such recommendations. This means that we contribute to what boards themselves can control and change to increase board task involvement. Compared to the dominant approach in the literature, this provides a more flexible and less deterministic notion of board work in small firms. We are therefore able to provide actionable advice to small firm owner-managers that consider activating their board.

The article is structured as follows. First we present a brief introduction of board tasks in small firms before we position the empirical study in relation to the 'usual suspects', board member motivation and board structures. Seven hypotheses are formulated. Then, we present our sample, the methods we used to collect and analyse the data and how we operationalized our variables. After presenting the results, a discussion is provided before the article ends with our key conclusions, suggestions for future research and practical implications.

2. Boards in the Small Firm: Theory and Hypotheses

In the governance literature the rationale for having boards of directors is associated with value creation and different tasks, where the tasks are often related to specific theoretical perspectives (e.g. Johnson et al., 1996; McNulty & Pettigrew, 1999; Zahra & Pearce, 1989). Agency theory is typically associated with control tasks and has its roots in the separation of ownership and control in large corporations. The control tasks broadly refer to monitoring on behalf of shareholders and other stakeholders. It has been argued that board members are less involved in control tasks in small firms (Forbes & Milliken, 1999; Gabrielsson & Winlund, 2000) than in large corporations. However, further agency theory reasoning and empirical evidence have shown that also boards in small firms may be involved in control tasks (Gabrielsson & Huse, 2005)

Resource dependence theory (Daily et al., 2003; Pfeffer, 1972; Pfeffer & Salancik, 1978) is about resource provision and is associated with how boards and board members provide service through networks and legitimacy to the firm and the top management.

The resource and knowledge-based view of the firm (Barney, 1991; Wernerfelt, 1984; Zahra & Filatotchev, 2004) supports a third main task of the board – strategy. From this perspective, the tasks of the board go beyond ratifying and controlling strategic decisions. They also include involvement in formulating the context and content of strategies, as well as being involved in the conduct of strategies (McNulty

& Pettigrew, 1999). The service and strategy tasks are considered to be particularly relevant in the context of small firms (Brunninge et al., 2006; Castaldi & Wortman, 1984).

Board Composition and the 'Usual Suspects'

The four dominating variables in board research are the number of board members, the insider/outsider ratio, CEO duality and shareholding by board members. These have been labeled as 'the usual suspects' (Finkelstein & Mooney, 2003) and researchers have been encouraged to find new variables to advance the knowledge about boards. However, as boards in small firms have received only limited attention, it is still relevant to test hypotheses between the 'usual suspects' and board task involvement.

The first and most studied 'usual suspect' is the board size. The number of board members is generally expected to have an inverse U-form relationship to firm performance (Zahra et al., 2000). Optimal board size is often considered to be between five and eight members. Many small firm boards have fewer members and are dominated by owner-managers' families and friends or professional advisors (e.g. accountants or attorney).

This may lead to limited board member independence and vigilance. From this perspective, increasing the number of board members increases the ability of the board to both service and control the top management. Resource dependence theory further suggests that a large board provides access to a wider range of useful resources external to the firm. Cowling (2003) finds that the number of board members in small firms is positively related to board activity. In other words, predictions from both agency theory and resource dependence theory lead us to suggest the following hypotheses:

H1 There is a positive relationship between the number of board members and board task involvement.

From an agency theory perspective, the insider/outsider ratio is used to measure board independence. Top management team members and their families are usually considered to be financially and psychologically dependent on the CEO. As such they are considered as insiders, and they are not expected to have sufficient distance to control managerial behavior and opportunism.

Earlier studies have shown that outsiders can make boards in small firms more active (Cowling, 2003; Johannisson & Huse, 2000). From a resource dependence perspective, the inclusion of non-executive board members may increase the availability of resources for a firm, and the number of outsiders will thus accordingly be positively related to board task involvement (Zahra & Pearce, 1989). Outside directors have thus potentially large contributions in small firms regardless of the theoretical perspectives employed (Gabrielsson & Huse, 2005). This is the case for family businesses and venture-capital financed firms, as well as for other small firms. We thus hypothesize:

H2 There is a positive relationship between the ratio of outside board members and board task involvement.

CEO duality exists when the CEO is also the board chairperson. It has been argued in the leadership literature that CEO duality may be positively related to firm performance because it secures unitary leadership. However, a core element in agency theory is the separation of control and executive tasks. Agency theory predictions will include a negative relationship between CEO duality and control tasks. CEO duality is particularly common in small firms as a result of the overlap between the owners, the board members and the top management team. Boards are expected to be less active and more informal when there is CEO duality (Nordqvist & Melin, 2002). Zahra et al. (2000) also found that CEO duality was negatively related to corporate innovation in medium-sized companies. Therefore:

H3 There is a negative relationship between CEO duality and board task involvement.

In the agency theory literature, shareholding by board members is considered to be one of the main criteria for board task involvement and in particular board control involvement (Kosnik, 1987; 1990). Board members' shareholding is believed to increase their motivation to get involved in control, service and strategy tasks (Johnson et al., 1993; Zahra et al., 2000; Zahra & Pearce, 1989). Shareholding board members, since they benefit from the firm's increased value-creation, are more prone to challenge the CEO and to seek in-depth knowledge about the firm and its environment (Zahra et al., 2000). This leads us to formulate the following hypothesis:

H4 There is a positive relationship between shareholding by the board members and board task involvement.

Board Members' Intrinsic Motivation

It is not enough that board members have knowledge and skills (Forbes & Milliken, 1999). They must also be motivated to use it. There are various reasons for board members to be active. Board shareholding, liability and personal or professional standards are suggested to be the most important motivational issues relating to board task involvement (Fama & Jensen, 1983; Hermalin & Weisbach, 1991). Shareholding is one of the usual suspects and it is included in hypothesis 4. Liability issues are first of all related to firms in financial crisis. Personal and professional standards are related to the market for board members and managers. The reputation of the board members will increase and their value in the market for board members and managers will also increase if they do a good job, but at the same time it will be at risk if they fail. From a resource dependence perspective, this may be especially relevant for outside board members since they use their reputation, networks and expertise to provide access to resources available outside of the firm (Borch & Huse, 1993). Moreover, in small firms the often close and

long-lasting ties between board members, managers and owners may mean that they feel more related to and identify more with the owner-family (Huse, 1993). This typically increases their motivation to be involved in board tasks. Gabrielsson & Winlund (2000) found evidence that in small firms committed and motivated board members mean greater involvement in both service and control tasks. Based on these theoretical and empirical arguments we therefore hypothesize:

H5 There is a positive relationship between board members' personal and professional motivation and board task involvement.

Board Working Structures

Boards in small firms typically meet only a few times every year, and the number of hours devoted to each board meeting is limited. However, for a board to perform well it is not enough to have the very best and competent board members. The board members and the board must also have a working style or working structure that allows the board members to use their knowledge and skills (Demb & Neubauer, 1992; Forbes & Milliken, 1999; Gabrielsson & Winlund, 2000). The amount of time devoted to actual board work can significantly determine the degree to which boards fulfill their tasks (Forbes & Milliken, 1999; Lorsch & MacIver, 1989). An active board requires time for preparation and careful planning, but the number of hours spent in each board meeting is also considered to be important for board task involvement (Demb & Neubauer, 1992; Huse, 2003), and in particular for board strategy and service involvement (McNulty & Pettigrew, 1999). Spending time together in board meetings is an essential ingredient for virtuous boardroom dynamics and a creative and innovative board behavior. Time is often a main constraint for many board members, and in particular for board members who are CEOs of other companies. As stated by agency theory, these may spend sufficient time on quantitatively related control tasks, but other board tasks will be expected to suffer due to time constraints (Brunninge et al., 2006; Hitt et al., 1996). Longer meetings also support process-orientation and a board climate where many actors can voice their opinions (Huse et al., 2005). Outside board members cannot be expected to monitor the firm (Demb & Neubauer, 1992), be involved in strategic issues or reach effective decisions (Conger et al., 1998) if not given enough time in the board meetings to discuss and evaluate various alternatives. Therefore:

H6 There is a positive relationship between the length of the board meetings and board task involvement.

It has been argued that regular board evaluations positively support board task involvement (Conger et al., 1998; Demb & Neubauer, 1992; Lorsch, 1995; Minichilli et al., 2007). Board evaluations represent a formal routine that facilitates a process-oriented boardroom culture. Having such an evaluation system allows for regular follow up on board members contribution to the different board tasks, making it easier to detect inefficiencies, and to improve the board work (Lorsch,

1995). Board evaluations can be performed in different ways and for different purposes, defining different board evaluation systems through the critical questions 'who does what for whom and how' (Huse et al., 2005; Minichilli et al., 2007). Few studies have investigated the role of board evaluation in small firms. In small firms, board evaluations may help to define board members' tasks and to enhance the relationship between the board and the top management team (Conger et al., 1998; Gabrielsson & Winlund, 2000). Moreover, they make it easier to determine whether new resources such as knowledge, skills and relations with external stakeholders are needed to improve the board task involvement over time. In this way, board evaluations address the possibility that demands and focus of the board work can change over time (Lynall, Golden & Hillman, 2003). Based on these arguments we formulate the following hypothesis:

H7 There is a positive relationship between regular board evaluation and board task involvement.

Methods

A cross-sectional associative research design was used to test the hypotheses. We used a sample of 347 Norwegian firms having between five and thirty employees. Norway has a one-tier board system for small firms. The system generally includes employee representation on boards, and CEO duality is not allowed. It is compulsory for the board to delegate the daily operation of the firm to a separate management. However, employee representation is not compulsory for firms with less than 30 employees, and CEO duality can be practiced in small firms with a share capital of less than 3 million Norwegian crowns (about 500,000 USD). Most small firms have this option. A detailed description of the sample, the variables and validation is found in the appendix.

Variables

Variables in the hypotheses. Three sets of variables were developed to measure the hypothesized relationships: 1) the dependent variables measuring board activity and task involvement, 2) the 'usual suspects' measuring board composition, and 3) the board working style variables measuring board member motivation and innovative tools to develop good board practices.

The dependent variable in our hypotheses is board task involvement. Three specific board task involvement variables and one summary variable were developed. The three specific variables were: control involvement to explore agency theory predictions, service involvement to explore resource dependence theory predictions and strategy involvement to explore predictions from the resource based view of the firm. These three variables are the board involvement tasks that have been used the most in earlier research (Zahra & Pearce, 1989). The total board task involvement was constructed as the mean of the three specific board involvement tasks variables. The three specific tasks were made in two steps, and seventeen items

employed in various earlier studies were used in developing our board task involvement measure. A detailed description of the construction of the variables is found in the appendix.

The term 'usual suspects' has been used for the mostly used variables in studies of boards of directors. They are: the number of board members, the insider/outsider ratio of board members, CEO duality and the shareholding of the board members.

The board working style variables included measures about board members' motivation, the length of the board meetings and board evaluations. The board members' intrinsic motivation followed measures used in earlier studies about how board members are motivated by personal and professional standards to do a good job on the board. The length of board meetings was the number of hours that ordinary board meetings lasted in 2003. The measure of regular board evaluations were taken from a list in the survey containing questions about the implementation of good corporate governance practices.

Boards should not be studied without paying attention to the context of the firms, and certain contextual variables are frequently used in board research (Zahra & Pearce, 1989). In this article, we categorize control variables in two groups: board external factors and leadership factors. Frequently used board external factors are firm size (Brunninge et al., 2006; Huse, 2000), firm crisis (Lorsch & MacIver, 1989; Mace, 1971), firm age and life cycle (Brunninge et al., 2006), firm international activities and industry characteristics (Borch & Huse, 1993; Huse, 1990). Leadership factors include CEO characteristics and tenure (Boeker, 1989; 1997), ownership (Gabrielsson & Winlund, 2000; Zahra & Pearce, 1989; Zahra et al., 2000), and family involvement (Schulze et al., 2003).

We included eight *contextual control variables* in the study. A logarithmic transformation of the number of employees was used to measure firm size. Firm crisis was measured through a composite index of four items where the CEOs on a five-point Likert type scale evaluated the existence of firm crisis during the recent three years (alpha .70). Firm age was measured as a logarithmic transformation of the number of years the firm, regardless of type of incorporation, had existed. International activities variable was the mean of three items about the percentage of exports on sales, exports on revenue and working force located abroad (alpha .80). One Likert scale type item on expanding industry was used as our industry characteristics measure. CEO tenure in present position was our CEO attribute variable. The percentage of ownership by the CEO, the top management team and their families was used as our ownership variable. Because most small firms are family firms (Brunninge et al., 2006), we also included a measure about family involvement. The family involvement was measured by a dichotomous variable measuring if more generations from the family were involved in the firm.

The above description reveals that the variables have been exposed to various types and degrees of validation. In most cases we used multi-items, and often also multi-respondent validation took place. In some cases we also conducted validation analyses through other methods and other samples.

Analyses and Results

Multiple linear regression analyses were used in testing the hypotheses. Residual analyses were conducted, but no results were found that changed the main conclusions. Statistical conclusion validity can be found, but inferences to causal relationship must only be done with care when using cross-sectional data without longitudinal data. Causal relationships will be discussed in the interpretation of the results. Correlation coefficients between the independent variables are presented in table 1. The results of the linear regression analyses are presented in table 2. Five models are displayed in the table. Equation I has the total board task involvement as the dependent variable. Equations II, III and IV are sub-models of equation I and display the different theoretical perspectives. The dependent variables are board control involvement, board service involvement and board strategy involvement. Equation V has the number of board meeting as the dependent variable. The partial standardized regression coefficients (beta coefficients) for each of the equations in the full model are displayed in the table. The table also displays full model equation statistics and stepwise statistics. The stepwise statistics displayed are the change in F in each step of the analysis. The full model statistics show that all equations are significant with R-squares ranging from .47 to .58 and adjusted R-squares ranging from .19 to .31. These figures are higher than what is found in most studies on board tasks.

The beta-coefficients for the variables numbered 9-15 correspond to the seven hypotheses. The hypotheses about the 'usual suspects' (hypotheses 1-4) are not supported. Hypothesis 5 about the board members' intrinsic motivation (beta is .40), hypothesis 6 about the length of the board meetings (beta is .11), and hypothesis 7 about regular board evaluations (beta is .25) are generally supported.

Table 1: Correlation analysis

| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 | 14 | 15 |
|------------------------------|------|------|------|------|------|------|------|-----|------|-----|-----|------|------|------|------|
| 1. Size (In employees) | - | | | | | | | | | | | | | | |
| 2. Crisis (recent 3 years) | | - | | | | | | | | | | | | | |
| 3. Firm age (In years) | | | - | | | | | | | | | | | | |
| 4. International activity | | | | - | | | | | | | | | | | |
| 5. Expanding industry | | | | | - | | | | | | | | | | |
| 6. CEO tenure | | | | | | - | | | | | | | | | |
| 7. CEO/TMT ownership | | | | | | | - | | | | | | | | |
| 8. Active family generations | | | | | | | | - | | | | | | | |
| 9. Board members (number) | | | | | | | | | - | | | | | | |
| 10. Outsider ratio | | | | | | | | | | - | | | | | |
| 11. CEO duality | | | | | | | | | | | - | | | | |
| 12. Board ownership | | | | | | | | | | | | - | | | |
| 13. Intrinsic motivation | | | | | | | | | | | | | - | | |
| 14. Length of meetings | | | | | | | | | | | | | | - | |
| 15. Board evaluations | | | | | | | | | | | | | | | - |
| 16. Board meetings (number) | 20 | 14 | 00 | 03 | 11 | -06 | -31 | -15 | 35 | 22 | -22 | -20 | 00 | 10 | 06 |
| 17. Total task involvement | -01 | -01 | -01 | -10 | 14 | 10 | 11 | -04 | -11 | -09 | -01 | 10 | 46 | 12 | 36 |
| 18. Control tasks | 00 | -01 | -01 | -09 | 11 | 13 | 18 | 01 | -14 | -10 | 06 | 12 | 38 | 00 | 24 |
| 19. Service tasks | -00 | 02 | -03 | -05 | 16 | 03 | 04 | -03 | -08 | -08 | -02 | 06 | 36 | 15 | 27 |
| 20. Strategy tasks | -04 | -01 | 02 | -10 | 08 | 08 | 07 | -07 | -07 | -04 | -06 | 04 | 39 | 14 | 31 |
| Mean | 2.32 | 1.88 | 2.83 | 3.51 | 2.67 | 7.92 | 57.2 | .23 | 3.58 | .65 | .22 | 64.6 | 3.95 | 2.68 | 2.69 |
| St.dev | .62 | .91 | .87 | 11.8 | 1.14 | 7.27 | 43.9 | .42 | 1.42 | .33 | .42 | 42.1 | .96 | 1.68 | 1.24 |

Pearson's product-moment correlation coefficients. All correlations are decimals. Coefficient .10 = 5% two tailed significance. N=347

Source: Our research

Table 2: Regression analyses

| Beta coefficients in the full model | I Total task involvement | II Control involvement | III Service involvement | IV Strategy involvement | V Number of board meetings |
|--|--------------------------|------------------------|-------------------------|-------------------------|----------------------------|
| Step 1 External factors | | | | | |
| 1. Firm size | -.005 | .065 | -.088 | -.063 | .088+ |
| 2. Crisis | .039 | .016 | .051 | .047 | .140** |
| 3. Age | -.046 | -.086 | -.039 | .011 | .022 |
| 4. International | -.109* | -.076 | -.076 | -.109* | -.050 |
| 5. Expanding industry | .092+ | .073 | .102 | .040 | .092+ |
| Step 2 Leadership | | | | | |
| 6. CEO tenure | .068 | .088 | .000 | .062 | .054 |
| 7. CEO ownership (incl TMT and family) | .046 | .100 | -.023 | .051 | -.154* |
| 8. Family generations active in firm | -.089+ | -.055 | -.037 | -.106* | -.091+ |
| Step 3 Usual suspects | | | | | |
| 9. Number of board members H1 | -.040 | -.033 | -.028 | -.035 | .236*** |
| 10. Outsider ratio H2 | .003 | .005 | -.040 | .026 | .082 |
| 11. CEO duality H3 | -.017 | .033 | .004 | -.070 | -.087 |
| 12. Board ownership H4 | .081 | .080 | .068 | .041 | .034 |
| Step 4 Motivation | | | | | |
| 13. Board member intrinsic motivation H5 | .402*** | .338*** | .321*** | .328*** | .007 |
| Step 5 Board structures | | | | | |
| 14. Length of board meetings H6 | .113* | .005 | .130* | .133** | -.019 |
| 15. Regular board evaluations H7 | .248*** | .198*** | .199*** | .222*** | .085 |
| R | .583 | .500 | .475 | .505 | .468 |
| Adj R2 | .310 | .217 | .191 | .222 | .185 |
| F (sign) Full model | 11.40*** | 7.51*** | 6.55*** | 7.605*** | 6.38*** |
| F change each step | | | | | |
| Step 1 External factor | 2.11+ | 1.52 | 1.88+ | 1.34 | 5.05*** |
| Step 2 Leadership factors | 3.29+ | 6.22*** | .48 | 2.26+ | 10.15*** |
| Step 3 Usual suspects | .99 | .60 | .77 | 1.17 | 7.60*** |
| Step 4 Motivation | 91.70*** | 58.83*** | 54.00*** | 57.34*** | .245 |
| Step 5 Board structures | 17.85*** | 8.09*** | 11.89*** | 14.52*** | 1.45 |

+ = .1-level, * = .05-level, ** = .01-level, *** = .001-level

Source: Our research

However, one major difference is found when comparing the different theoretical perspectives. The length of the board meetings (hypothesis 6) is not related to the control task involvement, but the beta coefficients are significant in the equations for the service and strategy task involvement. Hypotheses 1-4 are not supported in any of the perspectives, but hypotheses 5 and 7 about motivation and evaluation are supported in all of them.

A very different picture is found if we measure board activity through the number of board meetings instead of board task involvement. The number of board members (hypothesis 1) is significantly related to the number of board meetings. We also found that some of the control variables were significantly related to the number of board meetings.

The results displayed in table 2 give a very clear picture. First, the figures with respect to the board members intrinsic motivation (hypothesis 5) and regular board evaluations (hypothesis 7) are extremely strong. The validation of the constructs measuring board intrinsic motivation and the existence of regular board evaluations were in our study limited, but the results were so strong that we could not see that the overall conclusions could be changed. Second, board task involvement and the number of board meetings are two very different indications of board activity, and what makes boards involved in task performance is very different from what impacts the number of board meetings.

Discussion

The purpose of this article was to address the lack of research that explores what makes boards in small firms active. In doing this, we went beyond the 'usual suspects' and investigated how the board members' intrinsic motivation, the length of the board meetings and regular board evaluations influence board task involvement.

Several important observations were made. First, we found that the 'usual suspects' hardly explained any of the variance in board task involvement in the small firms in our study. None of the partial coefficients between the number of board members, outsider ratio, CEO duality and the ownership by board members were significantly related to any of the board task involvement variables. This finding corresponds to results from various meta-analyses in large corporations on the impact of the 'usual suspects' on firm financial performance (Daily et al., 2003; Johnson et al., 1996). Our findings also correspond to the findings of Gabrielsson & Winlund (2000) in their study of board control and service involvement in small and medium sized firms. We found, however, that the 'usual suspects', and in particular the number of board members, were related to the number of board meetings.

A second key finding was the strong result about the board members' intrinsic motivation. This is not surprising when reviewing the literature on boards in large firms. It is a major point by various authors, including Fama & Jensen (1983), Hermalin & Weisbach (1991, 1998) and Lorsch & MacIver (1989), that there is a market for board members, and that this market is a major motivational factor for the individual board members. Our study adds interesting evidence from small firms to this large-firm focused literature. The work of Westphal & Khanna (2003) on social distancing indicates, however, that there will be social pressures on board members not to ask discerning questions that will be against the informal norms of the ruling elites. We found in our study that personal and professional motivation was also significantly related to control involvement. Our findings are similar to the

results presented by Borch & Huse (1993) who found that board members' intrinsic motivation had a major impact on board networking involvement. Our findings indicate that it is not enough for board members in small firms to be outsiders, to be present at board meetings and to have knowledge and skills. They should also, as Forbes & Milliken (1999) suggest, be motivated to use it actively in the actual board work. The motivation of board members is a challenging and important topic for further research.

A third finding was the impact of regular board evaluations. Board evaluations are considered to be a powerful tool to develop boards, and the introduction of regular evaluation systems is recommended in most codes of best practices. Few studies have empirically shown this impact. Gabrielsson & Winlund (2000), in their study of Swedish small and medium-sized firms, did not find any relations between formal board evaluations and the boards' service and control involvement. We found, however, that board evaluations have impact regardless of which theoretical perspectives is used.

The greater adoption of board evaluation systems during the five years between our study and the Gabrielsson & Winlund (2000) study may account for the differences in findings. The variations in results may also be related to how the questions were formulated in the studies. Formality and regularity are two different aspects of board evaluation systems. Further studies should explore in more detail the impact of various elements of board evaluation systems.

A fourth major finding was the impact of the length of the board meetings. One aspect of this finding is that the length of board meetings has an impact on board task involvement. Another aspect is that a prescription of effective working style will vary with theoretical perspective and board tasks.

The results indicate that on one side board involvement in strategy and service tasks requires long board meetings. On the other side, control involvement seems to be independent of the length of the board meetings. This observation brings the attention to the inner working of boards and boardroom dynamics.

This follows conclusions in studies on large firms indicating that boards' contribution in strategy to a large degree depend on creative and interactive board meetings where the board involvement goes beyond ratification and output control (Hitt et al., 1996; McNulty & Pettigrew, 1999).

Control activities are less time consuming than the service to top managers or the involvement in the strategic process. Control activities typically rely on "hard information" readily put together in formal documents and financial reporting and budgeting routines. Service and strategy activities are often more ambiguous, complex and time-consuming, since they refer to broader issues with general impact on the firm and its relation to its environment as suggested by Brunninge et al. (2006). The understanding of the boardroom culture and dynamics should receive more attention in future studies.

A fifth finding is the limited explanations found in the contextual control variables. This was the case both for the external factors and for the leadership factors. Among the few relations observed was the negative relationship between the

involvement of several family generations in the firm and strategy involvement. Strategic decision-making may in such firms take place in other arenas than the boardroom, for example in family councils or informal arenas, such as family dinners, coffee breaks, etc. (Nordqvist & Melin, 2002). A negative relationship between board task involvement and firm international activities was also indicated. Two alternative explanations for this observation should be explored further. First, small firms with heavy international activities may be passive subsidiary boards, and second, board members may be risk averse and enforce restrictions to creative and impulsive managers who want international expansions.

The limited explanation of the contextual control variables on board task involvement was contrasted by their explanation of the number of board meetings. Firm size, past crisis, expanding industry, CEO ownership and family generations all seem to be related to the number of board meetings. These observations indicate that board activity may be influenced by contextual variables, but these variables do explain the contribution of board activities.

We have used an empirical setting from Norway to investigate what makes boards in small firms active. It has been assumed that the small firm setting is very different compared to the setting of most studies of boards of directors, that is, large and publicly traded U.S. corporations.

Our findings are, however, similar to what could be expected from general board task literature and research. This is interesting given the assumed special characteristics of small firms, such as overlapping governance structures, lack of functional managerial competence and strong owner representation in the boardroom and in the top management team (Brunninge et al. 2006; Cowling, 2003). Board practices are supposed to vary between large and small firms. Our findings suggest that common practices generated from a large firm context also seem to be relevant in small firms.

Conclusion

We have explored what makes boards in small firms active and we have used various theoretical perspectives to understand board task involvement. In line with research on large corporation we did not get any support for the four hypotheses about the relationships between the 'usual suspects' and board task involvement. The study illustrates the importance of going beyond the 'usual suspects'. Hypotheses about positive relations between board members' intrinsic motivation, the length of board meetings, and regular board evaluations were supported.

A theoretical contribution from the study is that few differences existed across the various theoretical perspectives. Intrinsic motivation and regular board evaluations were positively related to all board tasks. The length of the board meetings, however, was not related to the control tasks, and the 'usual suspects' were not related to any of the tasks.

The article has various actionable implications for small firm owners and managers. Given that motivation has such a high influence on board task

involvement, the selection of outside board members becomes critical. What is relevant is not only the appropriateness of board members' knowledge and skill with respect to the requirements from the firm's competitive environment, but rather the use of such skills. Therefore, the selection procedure in small firms should take into account elements besides the directors' competences. In addition to the competence, owners of small firms should make sure that the board members are motivated and involved. This can be done in different ways.

One way is to explore to what extent a board member identifies with the goals, values and interests of the owners and managers. Given the influence of the owner and top managers in small firms, the lack of identification with their goals, values and interests is likely to constrain involvement.

The scheme of incentives for board members' motivation and commitment should also be strengthened by the introduction of regular board evaluations. We suggest that boards should regularly evaluate themselves, but also that they increasingly let external specialized agents make evaluations that can support board development.

Various directions for further research are possible. First, our results emphasizing board members' intrinsic motivation, process-oriented boardroom dynamics and board evaluations should lead to refinements and further developments of measures used to explore these concepts. Second, a cross sectional associative research design was chosen. Further studies should include longitudinal designs.

Third, the CEOs were the respondents of the main survey in this study. The results are as most other survey studies about boards biased in favor of CEO perceptions. Future studies should also include responses from other respondents.

3. Appendix: Description of Sample, Variables and Analyses

The sample was taken from a database on boards in small firms. The original data was collected in 2004 through an eight page questionnaire where responses were collected from CEOs. The questionnaires were sent to a random sample of 3000 small firms that according to the list of Market Select had between 5 and 30 employees, and sales between 5 million and 50 million Norwegian crowns (just below 1 million and 10 million USD as one Norwegian crown is close to 6 USD). There was not an ex ante indication of the existence of boards in the firms. Responses were received from 973 firms, and in 498 firms we received questions about boards of directors.

We found that the response rates were slightly related to firm size in two ways. 1) The total response rates were highest for the smallest firms. 2) The response rates on board questions were highest for the largest firms. In our final sample we only used responses from firms that reported that they per 1.1.2004 had 5-30 employees. We found in total 347 firms that had complete responses on all the 39 board related survey measures we used in our analyses.

The study's measures were validated through responses from a sample of 80 chairpersons in the firms where there was no CEO duality.

We also compared our findings with results from another database collected in 2003 on another sample, mostly on larger and medium sized firms, but some small firms were also included. The findings relating to firms with less than 30 employees were similar in both surveys.

4. Description of the Sample

The sample consisted of boards in Norwegian firms with 5-30 employees. The mean number of employees in the firms was 11.5. The median was 10. Mean sales were 21 million Norwegian crowns, while the median 13.5 million crowns (around 3.5 and 2 million USD).

Almost four percent of the firms had in 2003 sales of more than 50 million crowns (some less than 10 million USD). We found that 9% of the responding firms were in the finance and real estate industry, 67% in services, including 24% retailing, and 18% were in manufacturing.

The CEOs responded in 23% of the cases that it was a high-tech firm, and 43% of the firms were by the CEOs considered to be a family firm. Families had voting control in the boards of 48% of the firms, families were majority owners in 50% of the firms, families were represented in the board in 65% of the firms, and owning families were in top management positions in 58% of the firms.

Venture capitalists owned more than ten percent of the shares in nine percent of the firms. The mean age of the firms was 25 years and the medium age was 17 years. The founder was still active in the firm in 62% of the cases.

5. The Variables

Board task involvement: All items were measured on a 5 point Likert type scale where 5 was "strongly agree". We first developed measures of the six subtasks presented by Huse (2005).

Network and resource dependence tasks were measured by two items (alpha .77), advisory tasks were measured by four items (alpha .79), output or quantitative control tasks were measured by four items (alpha .89), behavioral or qualitative control tasks were measured by three items (alpha .84), strategic control tasks were measured by two items (alpha .90), and strategic management and mentoring tasks (alpha .84) were measured by two items. A confirmatory factor analysis was then conducted to validate the three specific board tasks. Results of the factor analysis are presented in table 3.

Table 3: appendix Board tasks: Factor analysis

| | Strategy | Control | Service |
|--|------------|------------|------------|
| Network and resource dependence tasks | .19 | .16 | .54 |
| Advisory and knowledge based tasks | .26 | .39 | .70 |
| Output and quantitative control | .30 | .65 | .27 |
| Behavioral and qualitative control | .24 | .67 | .26 |
| Strategic control | .84 | .27 | .29 |
| Strategy participation and mentoring tasks | .74 | .33 | .26 |

Extraction Method: Alpha Factoring.

Rotation Method: Varimax with Kaiser Normalization.

Source: Our research

The results show loadings on factors corresponding to the variables control involvement, service involvement and strategy involvement. Convergent and discriminant validity are displayed. Board control involvement was thus made as the mean of quantitative and qualitative control (mean 3.75, std dev .84), board service involvement was made as the mean of networking and advisory tasks (mean 3.21, std dev .86) and board strategy involvement was made as the mean of strategic control and strategic management (mean 3.36, std dev 1.04). Total board task involvement was the mean of board control, service and strategy involvement (mean 3.44, std dev .75).

Number of board meetings: The figures were collected through the questionnaire. We only included ordinary board meetings in 2003 taking place with physical presence of the board members. The mean number of board meetings was 4.42 (std dev 2.18). The responses from the CEOs were validated through data collected from a sample of chairpersons in the same firms. The correlation coefficient between the CEOs' and chairpersons' responses was .53.

The 'usual suspects': Data on variables were collected from the CEOs' responses from the questionnaire. Our measures included only board members with voting rights. The mean number of board members was 3.58. We used NEDs (non-executive director) ratio on the total number of directors as our measure of outsider ratio. NEDs were calculated as the total number of directors minus directors being members of the top management team. Employee directors are in our measure included as NEDs. The mean NED ratio in the studied firms was .65. CEO duality is the case when the CEO also has the position as board chair. It was CEO duality in 22% of the firms. Ownership by the full board was also collected by the questionnaire to the CEOs and validated through responses from the chair on a separate questionnaire (corr .69). The mean ownership by the board members was 65%.

The board working style variables were single items from the questionnaire to the CEOs. A five point Likert type scale was used. The board members' intrinsic motivation followed measures used in earlier studies (Borch & Huse, 1993; Huse, 1993). Responses were validated through a separate questionnaire to a sample of

chairpersons in the same firm. Correlation with responses from chairpersons was .32. The length of board meeting was the number of hours ordinary board meetings lasted in 2003 (corr .50 with chair responses). The mean length of the board meetings was about 2 hours and 40 minutes. The measure of regular board evaluations were taken from a list in the survey containing questions about the implementation of good corporate governance practices.

6. Statistical Analyses

Various residual tests were conducted to control for how the standard regression model was met. Multicollinearity existed only in few cases, and then mostly related to family business and ownership issues. Family business issues are significant in most small firms. This is displayed in table 1 through the high correlation coefficients between CEO/top management team ownership (variable 7) and the ownership by the full board (variable 12). There were high correlations between the CEO/TMT ownership and the other 'usual suspect' board composition variables (variables 9, 10 and 11). We also found high correlations between board ownership (variable 12) and the number of board members (variable 9), and that more generations are active in the firm (variable 8). We observed a high correlation between firm age (variable 3) and CEO tenure (variable 6).

The linear regression analyses were conducted stepwise in order to reduce potential flaws based on multicollinearity. In the first step we included the board external variables (variables 1-5 in table 1). The CEO and management related variables (variables 6-8) were included in step 2. The 'usual suspect' board composition variables (variables 9-12) were included in step 3. The board intrinsic motivation variable (variable 13) was entered in step 4, and the board working structure variables (variables 14-15) were included in step 5. When testing the hypotheses we thus combined the interpretation of F-change results in the linear regression with the beta coefficients in the full model (table 2), and the correlation coefficient displayed in table 1.

A comparison between the beta-coefficients in table 2 and the correlation coefficients in table 1 can indicate the existence of multicollinearity. No differences were found related to hypotheses 5, 6 and 7. Some of the correlations about the number of board meetings related to hypotheses 1-4 that were significant in table 1 are not significant in the regression analysis (table 2). However, the stepwise approach and the changes in F from one step to another reveal that the 'usual suspects' in sum do not contribute significantly in any of the board task involvement equations. However, they do so in the number of board meetings equation.

The stepwise approach showed an interesting picture. On the one side, step 1 about external control variables, step 2 about leadership, and step 3 about the 'usual suspects' (hypotheses 1-4) were not significant in the main equation about total board task involvement. However, all three steps were significant in the number of board meetings equation. Step 2 about leadership factors was significant in the

control task equation. On the other side, both step 4 about motivation (hypothesis 5) and step 5 about board structures (hypotheses 6-7) were significant in equation I (board task involvement), but not significant in equation V (number of board meetings).

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