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The Myth of American Corporate Governance

Does Board Independence Really Improve Firm's Performance?

One of the most prominent characters of today's model of American corporate governance is the strong belief that independent boards work more effectively for the stockholders' interests than do not-so-independent boards that include many inside directors. However, there is no empirical evidence in support of this belief that independent boards help companies to achieve better performance.

Corporate America Shifted to Independent Boards.

One of the most remarkable changes in the history of U.S. corporate governance during the last 30 years is the shift in the board structure – from boards with many inside directors to ones predominantly occupied by independent directors. Until around 1970, insiders numerically dominated boards of directors. For example, Baysinger and Butler[1] found 54% inside directors, 26% affiliated directors, and only 20% independent directors in a sample of 266 large firms in 1970. By 1980, the proportion of inside directors in the sample had dropped to 43% and the proportion of independent directors had risen to 31%. Similarly, Hermalin and Weisbach,[2] found that firms had 49% inside directors, 13% affiliated directors, and 38% independent directors in 1971. By 1983, inside directors had fallen to 34% and independent directors had grown to 54%. (See table 1)

The trend toward greater board independence continued. In 1991 Bhagat and Black [3]sample, a median firm has an eleven-member board with three inside directors, one affiliated director, and seven independent directors. In percentage, the median firm had 23% inside directors, 13% affiliated directors, and 64% independent directors. Furthermore, the 1997 Board Index of S&P 500 corporations, as measured by SpencerStuart,[4] shows that the mean number of inside directors at these firms had dropped from three to two, and 72%of the boards were dominated by independent directors.

Table 1. Change in insider and independent directors; 1970 to 1997 perspective.

	Baysinger & Butler		% Change	Hermalin & Weisbach		% Change	Bhagat & Black	SpencerStuart
Board Composition	1970	1980		1971	1983		1991	1997
Insider	54%	43%	-20%	49%	34%	-31%	23%	18%
Affiliated	26%	26%	0%	13%	12%	-8%	13%	10%
Indep.	20%	31%	55%	38%	54%	42%	64%	72%

[1] Barry Baysinger & Henry Butler, *Corporate Governance and the Board of Director: Performance Effects of Changes in Board Composition*, 1 J.L. ECON. & ORG. 101 (1985).

[2] Benjamin E. Hermalin & Michael S. Weisbach, *The Effect of Board Composition and Direct Incentives on Firm Performance*, FIN. MGMT, Winter 1991, at 101.

[3] Bhagat, Sanjai and Black, Bernard S., "The Uncertain Relationship Between Board Composition and Firm Performance" . As published in Business Lawyer, Vol. 54, pp. 921-963, 1999. Available at SSRN: http://ssrn.com/abstract=11417

[4] Source: SpencerStuart, *1997 Board Index: Board Trends and Practices at S&P 500 Corporations.*

The lessons from the M&A boom that created conglomerates in the 70s and 80s.

This shift in board structure has been based on the conventional wisdom that independent boards work more appropriately according to the interests of the stockholders. Also, legal pressures and increasing M&A activities accelerated this shift. In order to understand why this shift happened, it helps to take a look at the serious debate on corporate governance that took place in the 1980s.

During the 1970s and 1980s, the U.S. experienced a wave of mergers and acquisitions. In the 1980s, the takeover activities were characterized by large-size, large-value 'mega deals.' The acquiring diversified and expanded their businesses in size and scope. American corporations became large in terms of sales and assets. However, this M&A boom to create conglomerates resulted in the deterioration of corporate profitability and damaged the shareholder's interests. The conventional wisdom and the legal and pressures derived from these failed merger activities, which were thought to have been motivated by managerial self-interest to seek bigger enterprises as opposed to the shareholders' interests to seek higher return on their investments. This provoked serious debate about corporate governance and how to saddle boards to work for shareholders' interest.

By the late 1980's, investors began to take actions to designate boards of directors to act on their behalf and to monitor management. They decided that the board was to ensure that management focuses on corporate profit maximization, and to provide guidance through key strategic decision-making process aimed at shareholder gains. But how were they to achieve this goal? One hopeful option, it seemed like, was to increase the number of independent directors on the board who were free from conflicts of interest. The courts picked up and supported this trend. For example, the Delaware Supreme Court encouraged majority-independent boards by being more lenient and agreeable towards decisions made by such shareholder-oriented boards. Interestingly, even banks became more likely to give credit to companies with an independent board. As a result, American corporations began to review and change their board composition based on such investors' demands.

Impact of the corporate scandals in 2001: Do independent boards really work for the shareholders?

Many corporate scandals represented by Enron and WorldCom frauds, however, revealed that boards, which had been considered independent, actually were not so. They did not have any checking power to stop the CEOs' egregious acts damaging the shareholders' interest. This is best exemplified by the 2001 Enron scandal, in which case Enron already had a super-majority independent board with only one insider, the CEO, who still managed to commit fraud.

In 2002 the U.S. Congress responded to these shocking scandals by following the conventional wisdom. The lawmakers passed the Sarbanes-Oxley Act (SOX) with aspirations to eliminate corporate frauds and improve corporate governance by introducing more strict standards for "independent directors." Also NYSE and NASDAQ set the rule which require the listed companies to have a majority of independence directors.

The Sarbanes-Oxley Act of 2002 was an instinctive response to frauds committed by largest American companies. But the proposed regulations were approved without proper empirical research on the benefits of independent boards. Despite conventional wisdom that companies with majority or super-majority independent board of directors make companies behave and perform better, many empirical studies show that there is no correlation between the share of independent directors in board composition and company performance. To this day, companies with or without majority independent boards continue to hide losses, overstate earnings, and mislead the boards, the shareholders, and the public. Corporate fraud continues regardless of the SOX and its attempt to minimize frauds and maximize investors' control through the board independence requirements.

No Correlation between board independence and companies' performance

A number of studies on the correlation between the share of independent directors in boards and company performance show that there are no meaningful relations between board independence and company performance. The empirical studies using financial statements show that board independence is unrelated to the company performance, earnings management and fraud detection. For example, the well-known studies by Baysinger and Butler[5], Hermalin and Weisbach[6], MacAvoy and co-authors[7] all report no significant same-year correlations between board composition and various measures of corporate performance.

The most respected is a study by Bhagat and Black,[8] which found that board independence and firm performance relationship may actually be negative (Tables 2 & 3). They reviewed various performance variables on board independence and stock ownership for 928 large U.S. public companies during 1988-1990 and 1991-1993. They utilized Tobin's q (Q)[9], the ratio of operating income to assets (OPI/AST), and the ratio of sales to assets (SAL/AST) as the performance measures variables. Table 2 shows the performance measures variables described above as a factor dependent on others. In that, the board independence (*INDEP*), most strongly affects the performance variables. The relationship is indeed significant, as shown in boldface, and is actually *negative*. As noted, the results show evidence that firms with a more independent board do not perform better, and hint that these firms suffer worse performance than those with a less independent board.

Truth is opposite: A firm's poor performance increases board independence.

Table 3, on the other hand, shows the board independence as the dependent variable. Here, the creation of independent boards is influenced by other variables. It turns out that a firm's poor performance increases board independence. Poorly performing firms increase board independence by thinking that this action will improve their performance. However, such a decision is vain as evidence shows that on average the performance does not change. The comparison of year-end in 1990 and year-end in 1993 indicates that the performance does not improve with greater board independence. While independent boards are a result of poor performance in companies, they do not improve that performance over time. The study concludes, "Whatever reasons prompt poorly performing companies to increase board independence, this strategy does not improve their future performance."

Investors' belief causes a share price premium of companies considered "well-governed".

Many institutional investors believe that a "monitoring board" composed of independent directors, is an important component of good corporate governance. Therefore, it is expected that the share price of those companies with a more independent board will be valued at a premium. Actually the studies, which use stock price return or bond yield as a method to measure corporate performance, find a positive link between board independence and company performance. The public rewards companies with independent directors by buying their stocks.

According "The Global Investor Opinion Survey" by McKinsey (2000 (updated in 2002)), 80% of the respondents said they would pay a premium for "well-governed" companies. Of course, here the investors think independent board is an important condition of "well-governed" companies. The size of the premium investors are willing to pay varied among markets: from 11% for Canadian companies to around 40% for companies

[5] *See* Baysinger & Butler, *supra* note 1

[6] *See* Hermalin & Weisbach, *supra* note 2

[7] Paul W. MacAvoy et al., *ALI Proposals for Increased Control of the Corporation by the Board of Directors: An Economic Analysis*, in BUSINESS ROUNDTABLE, (1983), BUSINESS ROUNDTABLE, STATEMENT ON CORPORATE GOVERNANCE 10 (1997), *at* http://www.brtable.org/pdf/11.pdf.

[8] Bhagat, Sanjai and Black, Bernard S., "The Non-Correlation Between Board Independence and Long-Term Firm Performance." As published in Journal of Corporation Law, Vol. 27, pp. 231-273, 2002 Available at SSRN: http://ssrn.com/abstract=313026

[9] The ratio of stock prices to the current replacement values of the firms' underlying assets.

operating in countries where the regulatory backdrop was less certain, such as Egypt, Morocco, and Russia. The UK and the US scored 12% and 14% respectively.

These opinion-based findings reflect a deep-seated belief amongst the public that “well-governed” companies which are represented by an independent board of directors supposedly run according to the shareholders’ interests and deliver better results. However, it is a common and erroneous belief that independent boards of directors guarantee better performance or better corporate governance. In the meantime, a bigger question remains unanswered. If the movement toward a more stockholders-oriented approach in corporate governance since the 80s was real, what was the real driving factor for this change? Further research is needed to answer this question.

End

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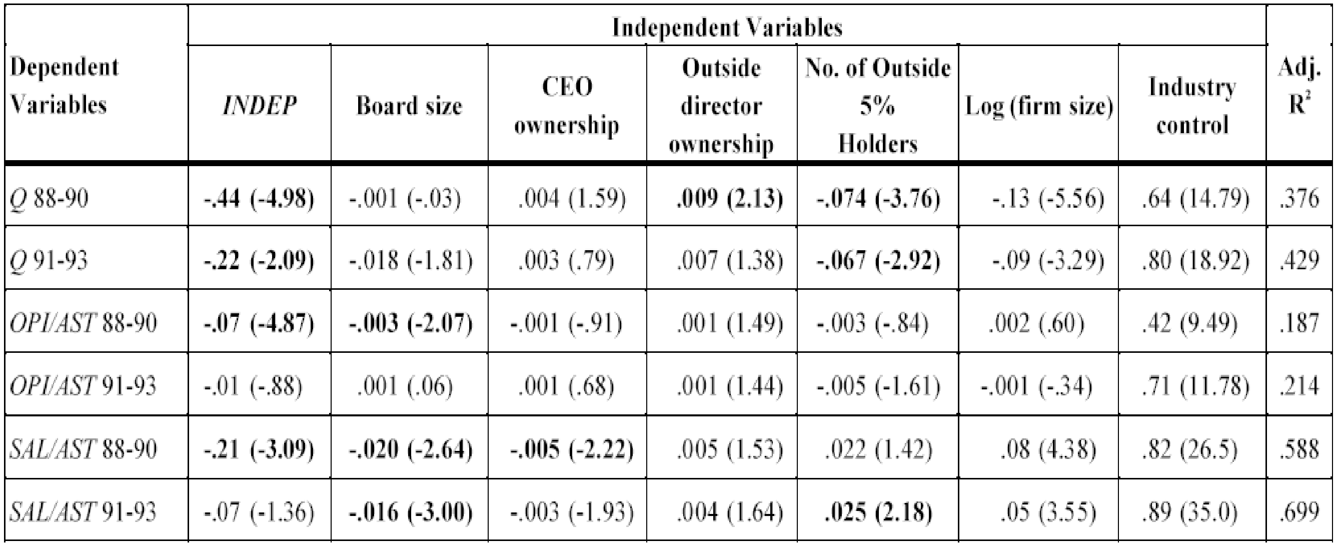
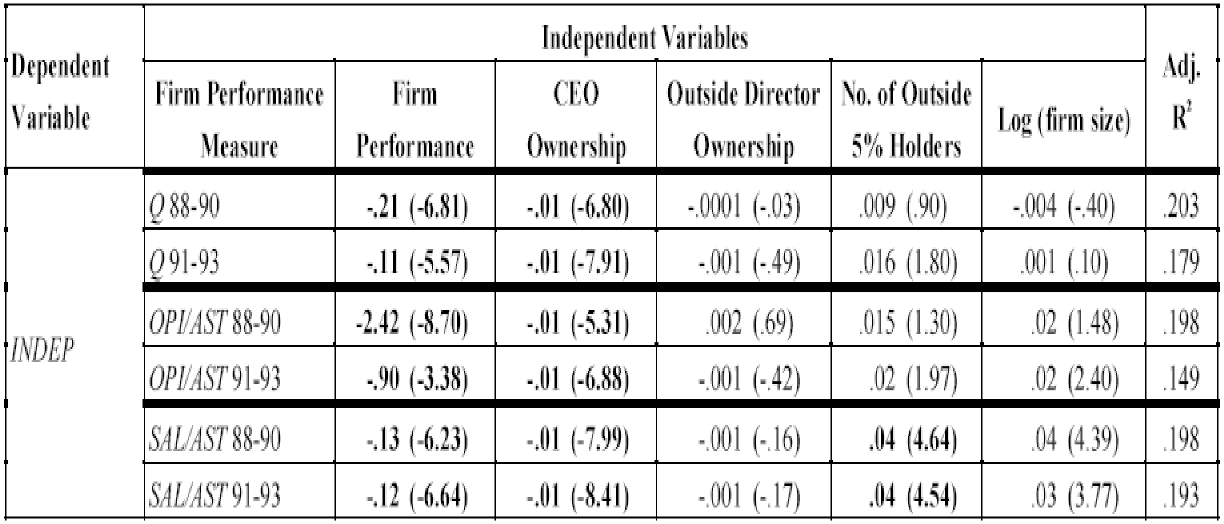
Table 2. Firm performance a dependent variable; shows board independence negatively affects firm performance.



Dependent Variables	Independent Variables							Adj. R^2
	INDEP	Board size	CEO ownership	Outside director ownership	No. of Outside 5% Holders	Log (firm size)	Industry control	
Q 88-90	**-.44 (-4.98)**	-.001 (-.03)	.004 (1.59)	**.009 (2.13)**	**-.074 (-3.76)**	-.13 (-5.56)	.64 (14.79)	.376
Q 91-93	**-.22 (-2.09)**	-.018 (-1.81)	.003 (.79)	.007 (1.38)	**-.067 (-2.92)**	-.09 (-3.29)	.80 (18.92)	.429
OPI/AST 88-90	**-.07 (-4.87)**	**-.003 (-2.07)**	-.001 (-.91)	.001 (1.49)	-.003 (-.84)	.002 (.60)	.42 (9.49)	.187
OPI/AST 91-93	-.01 (-.88)	.001 (.06)	.001 (.68)	.001 (1.44)	-.005 (-1.61)	-.001 (-.34)	.71 (11.78)	.214
SAL/AST 88-90	**-.21 (-3.09)**	**-.020 (-2.64)**	**-.005 (-2.22)**	.005 (1.53)	.022 (1.42)	.08 (4.38)	.82 (26.5)	.588
SAL/AST 91-93	-.07 (-1.36)	**-.016 (-3.00)**	-.003 (-1.93)	.004 (1.64)	**.025 (2.18)**	.05 (3.55)	.89 (35.0)	.699

Table 3. Board independence a dependent variable; shows that poor firm performance causes an increased board independence.



Dependent Variable	Independent Variables						Adj. R^2
	Firm Performance Measure	Firm Performance	CEO Ownership	Outside Director Ownership	No. of Outside 5% Holders	Log (firm size)	
INDEP	*Q* 88-90	-.21 (-6.81)	-.01 (-6.80)	-.0001 (-.03)	.009 (.90)	-.004 (-.40)	.203
	Q 91-93	-.11 (-5.57)	-.01 (-7.91)	-.001 (-.49)	.016 (1.80)	.001 (.10)	.179
	OPI/AST 88-90	-2.42 (-8.70)	-.01 (-5.31)	.002 (.69)	.015 (1.30)	.02 (1.48)	.198
	OPI/AST 91-93	-.90 (-3.38)	-.01 (-6.88)	-.001 (-.42)	.02 (1.97)	.02 (2.40)	.149
	SAL/AST 88-90	-.13 (-6.23)	-.01 (-7.99)	-.001 (-.16)	.04 (4.64)	.04 (4.39)	.198
	SAL/AST 91-93	-.12 (-6.64)	-.01 (-8.41)	-.001 (-.17)	.04 (4.54)	.03 (3.77)	.193

和文簡訳

米国コーポレートガバナンスの神話

～外部役員の増加は企業パフォーマンスを高めるか～

今日の米国のコーポレート･ガバナンス（企業統治）モデルのひとつの大きな特徴は、内部役員を多く含む取締役会よりも外部役員の割合の多い「独立性」の高い取締役会の方がより効果的に投資家の利益を実現するという通念である。ところが米国の多くの研究者による調査は、このような通念が実証的なデータからは支持されないことを示している。

外部役員からなる独立取締役会へのシフト

米国のコーポレートガバナンスの過去 30 年の歴史において、最も注目すべき変化は取締役会の構成変化である。1970 年頃までは取締役会の大部分を内部役員が占め、外部（独立）役員の割合は約 20～30％程度に過ぎなかった。しかし 1970～90 年代を通して、取締役会における外部役員の比率は上昇し、1997 年に Spencer Stuart が S&P 500 社を対象に行った調査では、取締役会の外部役員の比率は平均 72％となった。

1970-80 年代の M&A ブームにおける教訓

この取締役会構成の変化は、「外部役員をより多く含む独立性の高い取締役会ほど株主利益の実現に忠実である」という一般通念に根ざしているが、実際に取締役会構成の変化が生じた経緯については、70 年－80 年代の M&A ブームと当時のコーポレートガバナンスを巡る深刻な議論を理解する必要がある。

米国は 1970-80 年代にも M&A ブームを経験し、特に 1980 年代に M&A は大規模化した。当時の M&A は大規模複合企業を指向する傾向が顕著であったが、多くの場合、規模拡大に伴って企業の収益性は低下し、株主利益が損なわれる結果をもたらした。こうした複合大規模化を目指した M&A ブームの失敗は、それが株主の利益のためではなく、事業の巨大化自体を指向する経営者の自己利益に基づいていたと考えられるようになり、コーポレートガバナンスのあり方を巡る深刻な議論が展開した。

1980 年代の後半までには、専ら株主利益のために働く経営者を指名し、経営を監視する株主の活動が活発となった。株主らがその目的を実現する方策が、企業内部の利害から独立した社外役員の比率を増やすことだと考えられた。判例を通じた司法の判断もこうした動きを支持し、例えばデラウエアー州の最高裁は株主利益に奉仕する取締役会の構成として社外役員が多数を占めることを奨励した。こうした結果、米国では社外役員比率が大幅に引上げられる方向に取締役会構成の見直しが進んだのである。

2001年に続発した企業スキャンダルの衝撃

しかし、2001 年に起こったエンロンやワールドコムなど一連の企業会計スキャンダルは、独立性を高めたはずであった取締役会は、実際にはそうではなかったことを明らかにした。これら企業の取締役会は、株主利益を損なう経営幹部の不正行為を見抜き、止めさせる力を持っていなかった。特にエンロン事件はこの点で象徴的であり、エンロンは CEO を除くと全て社外役員で構成されていたが、不正は防止できなかった。

こうした事態への連邦議会は、やはり「独立性の高い取締役会ほど株主の利益追求に忠実」という一般通念に基づいたものであった。2002 年に連邦議会は Sarbanes-Oxley Act (SOX)法を可決し、より厳しい「取締役員

会の独立性の要件」を制定した。 NYSE や NASDAQ も上場企業に対して役員会の多数を社外役員とすることを義務付ける規則を設定した。

Sarbanes-Oxley Act (SOX)法は企業の不正行為の続発という衝撃的な事態に対する一般通念に基づいた議会の「本能的な対応」であったといえる。同法による規制は、「独立した取締役会」に関する適切な実証的調査が行われることなしに承認された。ところが、多くの実証的な調査・研究は、取締役会の構成と企業のパフォーマンスは無関係であることを示している。実際は、取締役会の過半数が外部役員である企業も、そうでない企業も会計不正行為を行ってきたのである。

取締役会の独立性と企業パフォーマンスの関係

取締役会の独立性と企業パフォーマンスの関係を調べた調査報告書はいくつか存在するが、その多くは両者は無関係であることを示している。それどころか、Sanjai Bhagat と Bernard S. Black が行った調査では、取締役会の独立性が高い企業ほどパフォーマンスは低いという結果が出ている。彼らの調査は、88－90 年、91－93 年の期間について、米国の 928 の大企業に対して、役員会の独立性と複数の指標による企業パフォーマンスの関係を検証したものである。パフォーマンス指標は、資産に対する営業利益率、資産に対する売上げ比率、トービンのQ（＝（企業株式の時価総額＋債務総額）/資本の再取得価格））などである。役員会の独立性を独立変数、企業パフォーマンスを従属変数として計測した結果、両者の関係は顕著にネガティブであった。

反対に企業パフォーマンス指標を独立変数とし、取締役会の独立性を従属変数とした計測では、パフォーマンスの悪い企業ほど取締役会の独立性を高める傾向が顕著であった。これは企業パフォーマンスの悪さを、社外役員の比率を高め、取締役会の独立性を高めることで改善しようとする動きが働いていることを示唆している。ただし、その結果パフォーマンスは改善しなかったことも確認されている。

投資家の通念がもたらす株価のプレミアム

多くの機関投資家は、独立した取締役会を持つことはコーポレートガバナンス強化の評価上重要なポイントであると考えている。それ故に、独立した取締役会を持つ「優良企業」の株価はプレミアムがついているとさえ考えられる。実際、企業パフォーマンスを株価や社債利回りを用いて測定した調査では、取締役会の独立性と企業パフォーマンスは正の相関関係が見られる。また投資家を対象とした世論調査では、「独立性の高い取締役会を持つ企業の株式に対してはプレミアム価格を支払う」と答えた回答者は 80％に達した。独立した取締役会を持つ企業はより良いコーポレートガバナンスと企業パフォーマンスを実現するという投資家の通念は、実証的には否定されているにもかかわらず、まことに深く根ざしていると言えよう。　もっとも未回答の大きな問題が残っている。80 年代以降の米国における株主至上主義的な方向へのコーポレートガバナンスの変化が本物であるならば、一体どういう条件がこの変化を生み出したのか？　この問題は後日の課題としたい。

以上