

Cambridge University Press

978-1-107-01487-9 - Challenging Boardroom Homogeneity: Corporate Law, Governance, and Diversity

Aaron A. Dhir

Excerpt

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## 1

### Introduction: Homogeneous Corporate Governance Cultures

I feel in a couple of situations that were very, very critical, then I saw [the] difference between how men and women behave .... I've seen situations where the women were more willing to dig into the difficult questions and to really go to the bottom even if it was extremely painful for the rest of the board, but mostly for the CEO ... when it comes to the really difficult situations, [where] you think that the CEO has ... done something criminal ... [o]r you think that he has done something negligent, something that makes it such that you ... are unsure whether he's the suitable person to be in the driving seat.

– Interviewee 14

(Norwegian public company board director, woman)

[I]f ... a new category of society shall be given power, someone will have to give away that power .... And that is not an easy thing to do.

– Interviewee 3

(Norwegian public company board director, woman)

Berkshire does not have a policy regarding the consideration of diversity in identifying nominees for director. In identifying director nominees, the ... Committee does not seek diversity, however defined.

– Annual proxy statements of Berkshire Hathaway Inc (2010–2013)

The lack of gender parity in corporate boardrooms, and in the governance of economic institutions more generally, has ignited a heated global debate. In 2010, the International Monetary Fund's managing director Christine Lagarde (at the time, France's finance minister) drily quipped that the face of the global financial crisis would have had a very different complexion

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“if Lehman Brothers had been ‘Lehman Sisters.’”<sup>1</sup> While her comment was viewed favorably in some quarters,<sup>2</sup> it elicited scathing critique from others; some characterized it as “a kind of lazy, sugar-and-spice gender essentialism” and “a tedious slice of benevolent sexism.”<sup>3</sup> That same year, members of a French feminist direct action group crashed the annual shareholder meeting of the Fortune Global 500 firm Veolia Environnement. Sporting faux beards, they sarcastically asked the chief executive officer (CEO) whether it was “wise to allow women to define the strategy of a company, a task requiring intelligence, an ability to react, and coolheadedness?”<sup>4</sup> At the time, just one of the firm’s seventeen directors was a woman.<sup>5</sup>

Lagarde and others who have expressed similar sentiments have contemplated the paucity of women in positions of decision-making power and helped advance a dialogue over whether regulation might facilitate equality and improve governance.<sup>6</sup> Her comments, like the French feminists’ protests, highlight the key issues that inform conversations currently taking place internationally with respect to gender representation in corporate governance. Why are some groups well represented in corporate leadership positions while others are not? Would increased heterogeneity result in different financial outcomes or differences in how firms are managed? And should global regulators intervene with corrective measures that attempt to diversify corporate hierarchies, or would this represent an unjustified interference with market sovereignty? If intervention is warranted, what form should it take?

<sup>1</sup> Christine Lagarde, “Women, Power and the Challenge of the Financial Crisis”, *The New York Times* (10 May 2010), online: <<http://www.nytimes.com/2010/05/11/opinion/11iht-edlagarde.html?dbk>>. The governance of financial institutions is a distinct issue that is not the focus of this book. I use this example only to illustrate the breadth of the global conversation and as a springboard for the ensuing discussion of corporate board diversity.

<sup>2</sup> “In Praise of ... Women Bankers”, Editorial, *The Guardian* (9 October 2013), online: <[www.theguardian.com/commentisfree/2013/oct/09/women-bankers](http://www.theguardian.com/commentisfree/2013/oct/09/women-bankers)>.

<sup>3</sup> Ally Fogg, “Don’t Give Me This ‘If Lehman Sisters Had Been In Charge ...’ Nonsense”, *The Guardian* (17 September 2013), online: <[www.theguardian.com/commentisfree/2013/sep/17/dont-give-me-lehman-brothers-sisters-nonsense](http://www.theguardian.com/commentisfree/2013/sep/17/dont-give-me-lehman-brothers-sisters-nonsense)>.

<sup>4</sup> Tara Patel, “French Women Storm the Corporate Boardroom”, *Bloomberg Businessweek* (10 June 2010), online: <[http://www.businessweek.com/magazine/content/10\\_25/b4183015410606.htm](http://www.businessweek.com/magazine/content/10_25/b4183015410606.htm)>.

<sup>5</sup> *Ibid.*

<sup>6</sup> Lagarde herself has endorsed the use of mandatory quotas in the corporate context. See Leyla Boulton & Andrew Hill, “Lagarde Embraces Quotas at FT Conference”, *The Financial Times* (16 November 2010), online: <[www.ft.com/intl/cms/s/0/a219537c-f1b0-11df-bb5a-00144feab49a.html#axzzzzimxBtYC](http://www.ft.com/intl/cms/s/0/a219537c-f1b0-11df-bb5a-00144feab49a.html#axzzzzimxBtYC)>.

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Global statistics indicate that women are noticeably underrepresented on the boards of the world's most significant publicly traded corporations,<sup>7</sup> and that country-level progress generally is “slow” and “incremental.”<sup>8</sup> Regionally, Europe displays the most noteworthy movement toward balanced representation levels. North America lags behind Europe (with Canada trailing the United States), and Asia (especially Japan and China) remains virtually stagnant.<sup>9</sup> Norway, Sweden, and Finland exhibit the highest percentages of women in global boardrooms, at 40.9 percent, 27 percent, and 26.8 percent, respectively. In comparison, the United States sits at 16.9 percent and Canada at 12.1 percent.<sup>10</sup> Figure 1.1 presents the percentage of board seats women hold in forty-four countries from Europe, North America, Asia, the Middle East, South America, and Africa, as well as Australia.

These statistics have recently become the subject of regulatory attention, with states seeking to diversify the upper echelons of their corporate sectors by pursuing law-based ameliorative strategies. In this book, I evaluate the two primary approaches that states and regulators have adopted to date.<sup>11</sup> The first consists of board diversity quotas imposed by legislators, and related target-based initiatives. In their most potent form, these measures mandate particular levels of gender balance in the boardroom. The second, less interventionist strategy requires information disclosure. Rather than dictating a predetermined outcome, regulators ask corporations to report publicly on diversity-related governance practices in varying levels of detail.

In global policy dialogues, commentators and policymakers invoke different justifications in support of these diversification efforts. They frequently present economic rationales, the argument being that diversified boards may enhance organizational financial performance. Also important, albeit frequently overshadowed, are equality-based arguments. These justifications, in turn, engage some of the most fundamental issues of corporate theory. Questions of

<sup>7</sup> My analysis in this book centers on for-profit corporations that issue securities for public distribution and are the subject of securities regulation, although I also make reference to state-owned enterprises and privately held corporations.

<sup>8</sup> Kimberly Gladman & Michelle Lamb, “GMI Ratings’ 2013 Women on Boards Survey” (April 2013) at 1, online: GMI Ratings <<http://www3.gmiratings.com/home/2013/05/gmi-ratings-2013-women-on-boards-survey/>>.

<sup>9</sup> *Ibid.*

<sup>10</sup> Catalyst, “2013 Catalyst Census: Fortune 500 Women Board Directors” (10 December 2013) at 1, online: <[www.catalyst.org/system/files/2013\\_catalyst\\_census\\_fortune\\_500\\_women\\_board\\_directors.pdf](http://www.catalyst.org/system/files/2013_catalyst_census_fortune_500_women_board_directors.pdf)>; Catalyst, “2013 Catalyst Census: Financial Post 500 Women Board Directors” (3 March 2014) at 1, online: <[www.catalyst.org/system/files/2013\\_catalyst\\_census\\_financial\\_post\\_500\\_women\\_board\\_directors.pdf](http://www.catalyst.org/system/files/2013_catalyst_census_financial_post_500_women_board_directors.pdf)>.

<sup>11</sup> As noted in Chapter 3, these two approaches should not be viewed as alternatives – a number of countries contain overlapping regulatory mechanisms.

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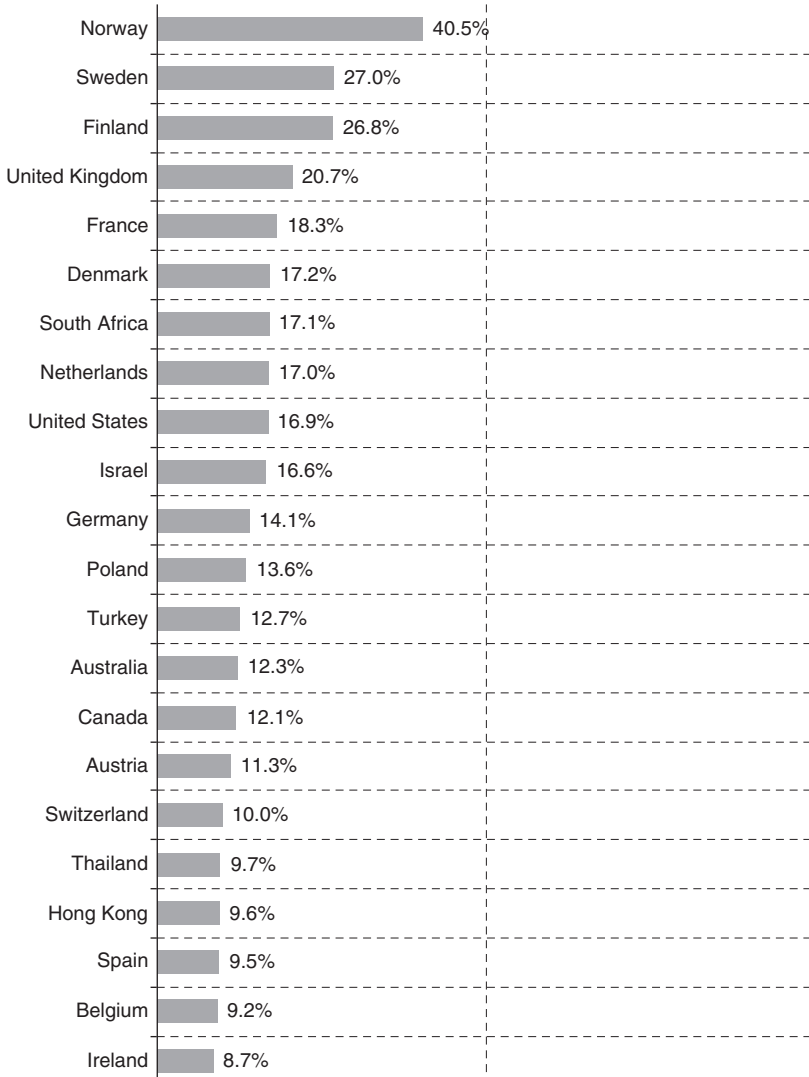
*Challenging Boardroom Homogeneity*

FIGURE 1.1. Percent of board seats women hold globally.

Source: Catalyst, Board Seats Held by Women, by Country. New York: Catalyst, April 29, 2014.

whether and how the state should seek to increase corporate governance diversity are strongly linked to competing conceptions of the corporate form. Is the firm's primary purpose to maximize the wealth of shareholders? Does it also exist to promote the general social welfare? While I am primarily concerned with how the regulatory mechanisms noted here operate in practice, I also examine their intersection with these underlying justifications. Most notably,

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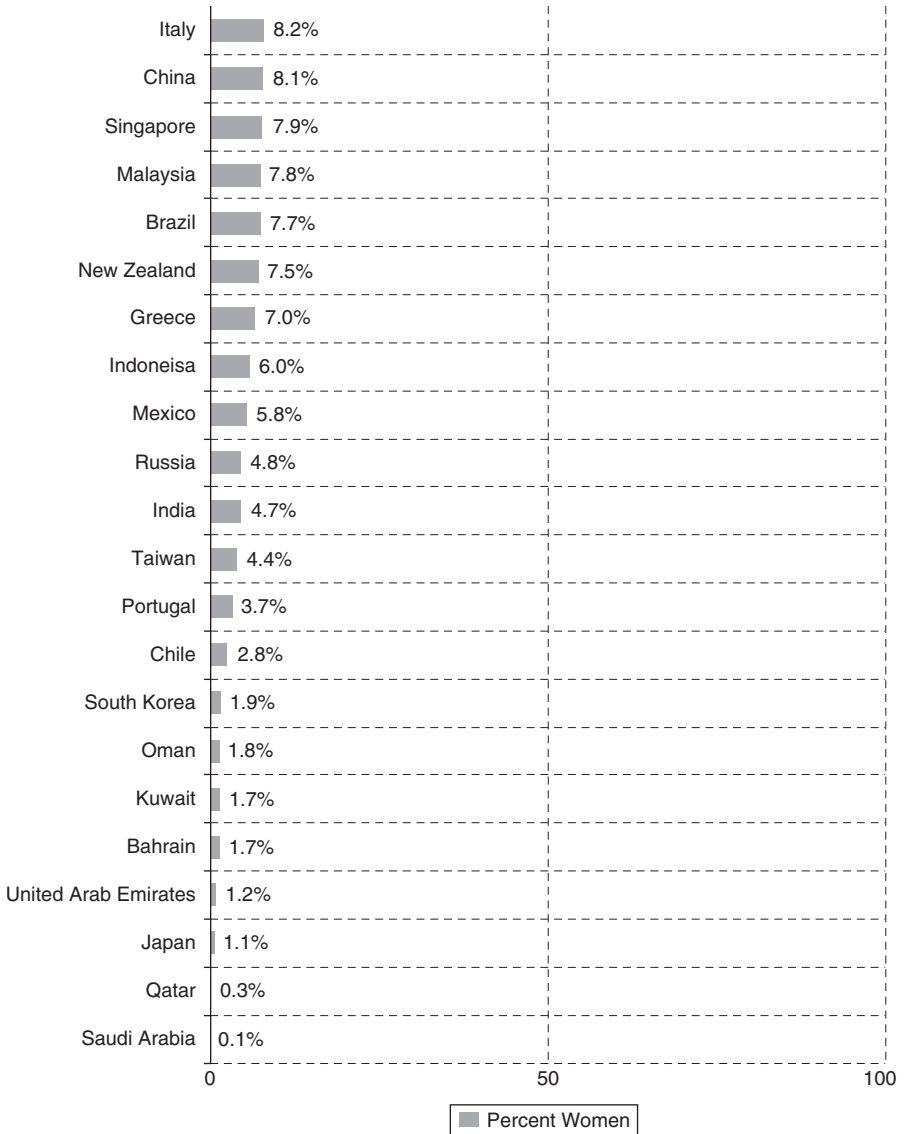
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FIGURE 1.1. (cont.)

I critically engage with instrumental, market-based reasoning. I argue that state-based intervention is essential to shifting existing norms, but should be based on a combination of factors related to organizational governance and decision making, and the goals of democratizing power and equitably distributing access to opportunities.

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VARIANCE IN CORPORATE GOVERNANCE MODELS AND  
THE MOVE TOWARD DIVERSITY REGULATION

The purpose of the corporate board and the board's relationship with other actors in corporate governance systems are not singular. Legal cultures in different jurisdictions envision the board playing varied roles. Factors such as the existing shareholder culture, particularly whether it is widely or closely held, and the degree to which the law recognizes the role of non-shareholder stakeholders, such as employees, creditors, and suppliers, inform the construction of these roles.<sup>12</sup> Similarly, boards exhibit structural variance. In the dual system, found in countries such as Germany, the Netherlands, and Austria, distinct supervisory and management boards perform the respective roles of overseeing and monitoring management and managing the firm's day-to-day business affairs. In the more common unitary system, exemplified by the United Kingdom, the United States, and Canada, a single board performs both roles.<sup>13</sup> Various jurisdictions afford firms the option to choose between a single- or two-tiered form,<sup>14</sup> and some, including the Nordic states, self-identify as lying "between" these regimes.<sup>15</sup>

Significant academic debate abounds on whether the forces of globalization will result in a convergence of corporate governance laws and norms toward a single model,<sup>16</sup> and in general "[c]orporate governance is on the reform agenda all over the world."<sup>17</sup> Board diversity-related reform represents an important component of the current dialogue. In all corporate governance cultures, dual or unitary, shareholder- or stakeholder-oriented, the reality is that states have

<sup>12</sup> Paul L Davies & Klaus J Hopt, "Corporate Boards in Europe – Accountability and Convergence" (2013) 61:2 Am J Comp L 301 at 302–03.

<sup>13</sup> Klaus J Hopt, "Comparative Corporate Governance: The State of the Art and International Regulation" in Andreas M Fleckner & Klaus J Hopt, eds, *Comparative Corporate Governance: A Functional and International Analysis* (New York: Cambridge University Press, 2013) 3 at 29–31.

<sup>14</sup> *Ibid* at 98.

<sup>15</sup> See the 2009 joint paper published by the corporate governance agencies of Norway, Finland, Denmark, Sweden, and Iceland. Danish Corporate Governance Committee et al, "Corporate Governance in the Nordic Countries" (April 2009) at 8, online: Iceland Chamber of Commerce <[www.vi.is/files/Nordic%20CC%20-%20web\\_1472238902.pdf](http://www.vi.is/files/Nordic%20CC%20-%20web_1472238902.pdf)> ("The Nordic corporate governance structure lies between the Anglo-Saxon one-tier and the continental European two-tier model.").

<sup>16</sup> The pro-convergence argument is most notably, and controversially, advanced in Henry Hansmann & Reinier Kraakman, "The End of History for Corporate Law" (2001) 89:2 Geo LJ 439 at 468 (arguing "the triumph" and "ideological hegemony" of the Anglo-American shareholder-focused structure).

<sup>17</sup> Jeffrey N Gordon & Mark J Roe, "Introduction" in Jeffrey N Gordon & Mark J Roe, eds, *Convergence and Persistence in Corporate Governance* (Cambridge, UK: Cambridge University Press, 2004) 1 at 1.

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now begun tackling the difficult questions noted in the previous section. And in doing so, momentum is building toward the adoption of law-based or “law like” structures,<sup>18</sup> in both common and civil law jurisdictions. While such reform has appeared primarily in developed economies, initiatives (or proposed initiatives) in countries such as India, Kenya, Malawi, the United Arab Emirates, and South Africa suggest that this trend has reached developing economies as well.<sup>19</sup>

These developments underscore that the dynamics of international economic activity do not exist in isolation, but are integral components of a broader societal landscape.<sup>20</sup> In understanding how corporations are situated, it is useful to call to mind the intellectual project of Hungarian economic historian Karl Polanyi, who shows society and the market to be in a state of “related tension.”<sup>21</sup> The market is embedded within the society, and in order to protect against the risks that follow self-interested gain, “market societies must construct elaborate rules and institutional structures.”<sup>22</sup> This dynamic constitutes Polanyi’s “double movement” thesis: as the negative effects of economic activity emerge, protective reactions emanate from society. These reactions resist efforts to decontextualize the economy from societal institutions.<sup>23</sup> Block discusses these themes by invoking the image of a rubber band. Attempts to enhance market sovereignty raise the degree of tension as the band is stretched. As this elongation continues, the band will eventually break, resulting in social dissolution, or retract, resulting in the market going back to an embedded state.<sup>24</sup>

<sup>18</sup> Davies & Hopt, *supra* note 12 at 327. See also Massimo Belcredi & Guido Ferrarini, “Corporate Boards, Incentive Pay and Shareholder Activism in Europe: Main Issues and Policy Perspectives” in Massimo Belcredi & Guido Ferrarini, eds, *Boards and Shareholders in European Listed Companies: Facts, Context and Post-Crisis Reforms* (Cambridge, UK: Cambridge University Press, 2013) 1 at 28 (“[R]egulation is the single most important factor explaining differences in board gender diversity across European countries.”).

<sup>19</sup> Further details are provided in the final section of this chapter and in Chapters 3 and 7.

<sup>20</sup> Amanda Perry-Kessaris, “What Does it Mean to Take A Socio-Legal Approach to International Economic Law?” in Amanda Perry-Kessaris, ed, *Socio-Legal Approaches to International Economic Law: Text, Context, Subtext* (Oxfordshire: Routledge, 2013) 3 at 9.

<sup>21</sup> Mark Banks, “Karl Polanyi, The Rubberband Man” (12 December 2008), online: The Open University <<http://www.open2.net/blogs/society/index.php/2008/12/12/karl-polanyi-the-rubberband-man?blog=10>>.

<sup>22</sup> Fred Block, “Karl Polanyi and the Writing of *The Great Transformation*” (2003) 32:3 *Theory & Soc’y* 275 at 297.

<sup>23</sup> Karl Polanyi, *The Great Transformation: The Political and Economic Origins of Our Time* (New York: Farrar & Rinehart, 1944) at 76 (“While on the one hand markets spread all over the face of the globe ... on the other hand a network of measures and policies was integrated into powerful institutions designed to check the action of the market ... Society protected itself against the perils inherent in a self-regulating market system.”).

<sup>24</sup> Fred Block, “Introduction” in Karl Polanyi, *The Great Transformation: The Political and Economic Origins of Our Time*, 2d ed (Boston, Mass: Beacon Press, 2001) at xxv.

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This analytical structure has obvious applicability to debates on globalization, deregulation, and the financial crisis. But it is also relevant to corporate governance diversity. According to traditional economic theory, the market should eventually address and protect against biases related to sociodemographic status.<sup>25</sup> However, this proposition, to date, has not proven true at the highest levels of the corporation. Correspondingly, states have begun to impose regulatory and institutional frameworks that constrict unbridled market movements, thereby grounding the market in the “moral fabric of society.”<sup>26</sup> As noted in the first section of this chapter, and as I further discuss in subsequent chapters, the justifications for these interventions have not been solely (or even predominantly) predicated on equality-based grounds, but the interventions push in that direction nonetheless.

## ROADMAP OF SUBSEQUENT CHAPTERS

In this book, I focus on the corporate boardroom as a core location of power in the global marketplace.<sup>27</sup> I explore the boardroom as a site of contestation over sociodemographic diversity and as a place of social closure and social struggle. I consider who has been granted access to the highest levels of the corporate hierarchy, and, in recognizing the homogeneity of this site, I explore the ameliorative strategies states and regulators employ in an effort to alter the status quo. What shape have these initiatives taken and what has been their effect?

Fundamentally, this is a book about corporate governance – the “system by which companies are directed and controlled.”<sup>28</sup> Corporate governance has exploded as a subject of reflection in scholarly, policy, educational, and practitioner-based circles.<sup>29</sup> The degree of attention it attracts has only intensified in the wake of the global financial collapse.<sup>30</sup> As a field of intellectual

<sup>25</sup> Richard A Epstein, *Forbidden Grounds: The Case Against Employment Discrimination Laws* (Cambridge, Mass: Harvard University Press, 1992) at 9 (“Competitive markets with free entry offer better and more certain protection against invidious discrimination than any antidiscrimination law.”).

<sup>26</sup> Jens Beckert, “The Great Transformation of Embeddedness: Karl Polanyi and the New Economic Sociology” in Chris Hann & Keith Hart, eds, *Market and Society: The Great Transformation Today* (Cambridge, UK: Cambridge University Press, 2009) 38 at 41.

<sup>27</sup> “Boardroom – the word alone conjures up visions of power, wealth, and privilege.” Jay W Lorsch & Elizabeth MacIver, *Pawns or Potentates: The Reality of America’s Corporate Boards* (Boston, Mass: Harvard Business Review Press, 1989) at 1.

<sup>28</sup> Adrian Cadbury, *Report of the Committee on the Financial Aspects of Corporate Governance* (London: Gee, 1992) at para 2.5.

<sup>29</sup> Mike Wright et al, “Introduction” in Mike Wright et al, eds, *The Oxford Handbook of Corporate Governance* (Oxford, UK: Oxford University Press, 2013) 1 at 1.

<sup>30</sup> Hopt, *supra* note 13 at 5. For a review of the schools of thought on whether corporate governance structures and processes were a significant factor in the financial crisis, see William Sun, Jim



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inquiry, it is remarkably vast, with a wealth of literature from a range of academic traditions addressing the host “of legal, cultural, and institutional arrangements that determine what public corporations can do, who controls them, [and] how that control is exercised.”<sup>31</sup>

This book is also fundamentally about a set of questions that have received much less attention from legal scholars of the corporation: questions involving the social phenomenon of *diversity*. Diversity itself is an amorphous and heavily contested concept.<sup>32</sup> Construed expansively, it might encompass the full array of groups and persons that compose any given community.<sup>33</sup> Sociologists of culture, however, identify it as a “keyword” – a linguistic expression that possesses widely acknowledged connotations but is also “open to local interpretation” and dependent on context and “the social location of the speaker.”<sup>34</sup> As Schuck observes, diversity “means different things to different people” and can “mean different things even to the same person at a single point in time.”<sup>35</sup>

Because I am concerned with the sociodemographic homogeneity of corporate boards, this book focuses primarily on identity-based markers of diversity. In the field of corporate governance, international regulatory efforts aimed at diversification have largely involved gender. For that reason, much of this book necessarily considers the lack of women in the upper echelons of business corporations and the relationship between gender and economic governance.<sup>36</sup>

Chapter 2 lays the foundation for understanding recent regulatory innovations in three ways. I begin by considering why the international spotlight is

Stewart & David Pollard, “Introduction: Rethinking Corporate Governance – Lessons from the Global Financial Crisis” in William Sun, Jim Stewart & David Pollard, eds, *Corporate Governance and the Global Financial Crisis: International Perspectives* (New York: Cambridge University Press, 2011) 1 at 4–7.

<sup>31</sup> Margaret M Blair, *Ownership and Control: Rethinking Corporate Governance for the Twenty-First Century* (Washington, DC: The Brookings Institution, 1995) at 3.

<sup>32</sup> Joyce M Bell & Douglas Hartmann, “Diversity in Everyday Discourse: The Cultural Ambiguities and Consequences of ‘Happy Talk’” (2007) 72:6 Am Soc Rev 895 at 896 (“However defined, the concept of diversity has come under heavy scrutiny from public intellectuals.”).

<sup>33</sup> Faisal Bhabha, “Towards a Pedagogy of Diversity in Legal Education” 52:1 Osgoode Hall LJ [forthcoming in 2015] at 9.

<sup>34</sup> Ellen Berrey, “Bottom-Line Diversity: Race and Productive Pluralism in the Post-Civil Rights Era” (September 2012) at 27, online: SUNY-Buffalo <[www.acsu.buffalo.edu/~eberrey/index\\_files/Berrey-%20Bottom-Line%20Diversity-%20Intro,%20Chap%201,%20Chap%205,%20Sept%202012.pdf](http://www.acsu.buffalo.edu/~eberrey/index_files/Berrey-%20Bottom-Line%20Diversity-%20Intro,%20Chap%201,%20Chap%205,%20Sept%202012.pdf)>.

<sup>35</sup> Peter H Schuck, *Diversity in America: Keeping Government at a Safe Distance* (Cambridge, Mass: Harvard University Press, 2003) at 19.

<sup>36</sup> In choosing to focus this book on gender diversity at the highest levels of the firm, I acknowledge that I am concentrating on a small, privileged group that draws advantage from class differentials.

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focused on boards of directors in particular as sites for diversification. With an emphasis on the United States and Canada, I then consider possible explanations for existing low levels of representation. I question the narrative of a supply problem that often originates from firms and suggest that a more appropriate explanation lies in the coupling of implicit cognitive biases with the fact that the networks of existing directors are limited in scope and restrict entry. I close by evaluating the rationales for diversification. How has the reform-based discourse, to date, justified the push toward increased boardroom heterogeneity? I unpack the difficulties of the dominant “business case” for diversity and advocate an approach that centers on social equality, as well as on governance effectiveness and decision making, rather than on a consequentialist view of shareholder wealth maximization.

As noted, regulators have turned to formal remedial measures in an effort to curb the ubiquity of male-dominated corporate leadership structures. In Chapters 3 through 7 I present and situate the core original research of the book, focusing on the two primary modes of legal regulation adopted to date. Chapter 3 introduces corporate board quotas. I provide an overview of existing quota- and target-based regimes, teasing out their key characteristics and elucidating how these systems work. I then turn to corporate reporting. In 2009, the U.S. Securities and Exchange Commission (SEC) adopted a diversity disclosure rule that, among other things, asks publicly traded firms to report on whether they consider diversity in identifying director nominees. I examine the rule’s details and explore its conceptual underpinnings. I also address reactions to the rule and contend that, despite the controversy, the SEC did not stray significantly from its mandate when promulgating the rule.

Chapter 3 concludes by contextualizing these initiatives within wider bodies of regulatory thought. I present quotas as a form of command-and-control regulation, according to which the relationship between the regulator and the regulated is hierarchical and predicated on a deterrence-based logic. In contrast, disclosure represents a form of decentered, new governance regulation where the state no longer serves as the sole or primary regulator. Rather, it forms but one part of a pluralistic regulatory environment where the regulated entity and other non-state actors also contribute to the formulation of an overall normative ordering. In the case of quotas, the regulation of corporate governance diversity takes place at the state’s behest; with disclosure, it takes place more in the state’s shadow.<sup>37</sup>

<sup>37</sup> The shadow metaphor was recently used to great effect in Marc T Moore, *Corporate Governance in the Shadow of the State* (Oxford, UK: Hart Publishing, 2013).