Is a friendly board a better board?

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Research by UQ Business School's Professor Renée Adams suggests that increasing the independence of boards may not be so good for shareholders. Professor Adams and co-author Daniel Ferreira found that boards emphasising their monitoring role were less likely to have access to all relevant information.

“We found that friendly boards may be optimal,” Professor Adams said.

She said the emphasis on independence supported the monitoring role of the board but limited its ability to advise effectively.

“The dual role of boards in countries like the US and Australia complicates the relationship between management and the board,” she said.

“CEOs face a trade-off in disclosing information to the board – if they share information freely they can expect better advice.”

“However, information sharing also allows the board to monitor the CEO's role more closely.”

The paper (forthcoming in the *Journal of Finance*) analyses the differences between a sole board system, such as in the US and Australia, and the dual board system favoured by various European countries.

Professor Adams, and Mr Ferreira of Universidade Nova de Lisboa, used sophisticated mathematical modelling to explore four key ideas.

Professor Adams said the first idea was that the CEO may dislike some monitoring activities of the board because they impair his or her autonomy.

“But the advisory role of the board increases firm value without interfering with the CEO's choices so the CEO likes that aspect of the board's activities,” she said.

“And we know that both monitoring and advising are more effective when the board is well informed – and that the board depends on the CEO for information.”

She said the research showed that emphasising director independence may have adverse consequences in the sole board system but would "unambiguously" enhance shareholder value in a dual board system.

“By delegating monitoring roles to audit and remuneration committees, a sole board takes on the nature of a dual board. Thus, our results imply that emphasising independence of committee members is likely to result in good outcomes for shareholders,” Professor Adams said.

“But, when a management-friendly board is optimal, one should expect other governance mechanisms to pick up the slack.”

Source: University of Queensland