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The Morning Risk Report: Over-Committed Directors Good for Young Firms

By Mara Lemos Stein
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Directors that hold seats at multiple corporate boards may hurt a company's profitability, but they bring invaluable expertise and experience to young companies, and have a measurable positive impact on a young company's financial performance, recent academic research found.

Investors' concerns and academic studies about the risks of over-committed directors being less efficient abound, and have influenced a sharp decline in the number of directorships held in the U.S. to an average of three in 2012 from five in 1999, according to the paper published last month as part of the Georgia Tech Scheller College of Business research series. Proxy advisory firm Institutional Shareholder Services, for instance, recommends that directors shouldn't hold more than five appointments at public U.S. companies. The research, which looked at board composition at companies in more than 50 countries, found that "busy boards are a global phenomenon," with approximately 70% of firms having busy boards, or those with over-committed directors. But advocating for streamlining directorships in the U.S. can be misguided when it comes to young companies, said the paper's authors Stephen Ferris, of the University of Missouri, Narayanan Jayaraman, of Georgia Tech, and Min-Yu Stella Liao, of Illinois State University. "The advising and networking advantages associated with widely boarded directors is most useful for younger firms," the researchers wrote. For example, well-connected directors can provide critical insight into managing relations with investors and analysts, and with regulatory entities. "But as firms mature, it is likely that director monitoring of managers becomes even more important for the creation of profitability and shareholder value," it said, and that oversight may be compromised when directors are overburdened by multiple seats.

And the role of a director hasn't remained static, though, and has changed in the past 15 years, said Matteo Tonello, managing director for corporate leadership at the Conference Board, a membership organization. Besides growing investors' scrutiny, legal and regulatory developments over the period mean that boards "have become much more eclectic." They now have to perform certain tasks and oversight in regards to audit, compensation, risk and succession planning, among many others, which require a significant time commitment that goes beyond the regular meetings, he said. "Engaged and well-connected directors are important resources to a corporation," said Mr. Tonello. "[But] beyond a certain threshold, other directorships can translate into unmanageable distractions and negatively affect firm value."