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## BOARD COMPOSITION AND CONTROL: AN EXPLORATORY ANALYSIS OF ORGANIZATIONAL CRISIS AND PREVENTION

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*Despite extensive scholarship on the subject of board control, the scandals of recent years suggest the need to revisit our assumptions - and our theories - regarding alternative board control mechanisms. This study uses an exploratory factor analysis comparing firms that successfully or unsuccessfully avoided governance failure and the onset of crisis to assess the consistency of board structures. Results indicate that there is some consistency among the successful firms, but that in general no common structural form can be linked to either success or failure. Thus, general rules cannot be relied upon, and a context-specific approach to governance should be developed.*

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### INTRODUCTION

Agency theory's insights into the implications of the separation of ownership and control (Fama, 1980; Fama & Jensen, 1983a, 1983b; Jensen & Meckling, 1976) sparked significant interest in governance structures and the ability to delimit managerial authority. One of the more important aspects of governance, and one attracting increasing attention, is the board of directors, which is charged with exerting control over management on behalf of the firm's shareholders (Fama & Jensen, 1983a). A prodigious body of literature investigating boards' performance of the control function has developed (see, e.g., Daily et al., 1999; Dalton et al., 1998; Johnson, 1996; Johnson, Daily & Ellstrand, 1996; Pearce & Zahra, 1991; Zahra & Pearce, 1989), and with it expectations regarding board structures appropriate to the exercise of control. Despite such advances, and, increasingly, firms' implementation of many of these structural forms (e.g., Bhagat & Black, 2002; Hoskisson et al., 1994), we have witnessed an unparalleled number of scandals and blunders in recent years that clearly imply that observance of form is not necessarily a prerequisite to success.

Clearly, something is wrong, but the question of whether the fault lies with inadequate control systems or merely inappropriate implementation remains unanswered. And this question, in turn, raises the additional issue of whether our theories and prescriptions themselves are complete and sufficiently explanatory in all circumstances. In fact, several empirical analyses suggest that our understanding of the effects of board structure and composition is, at best, incomplete (e.g., Daily et al., 1999; Dalton et al., 1998; Deutsch, 2005; Rhoades et al., 2000). Moreover, no research has directly assessed these characteristics in the context of specific instances of governance failure in order to understand

how control mechanisms, and corresponding theory, might differ from one condition to another.

This article attempts to address these issues by examining the extent to which board structures are similar or different among firms facing various governance challenges. If our current theories produce uniform effects, there should be no differences among successful firms in any context. Likewise, those firms experiencing crisis and governance failure should have similar forms and structures among themselves, which in turn should differ from those of successful firms. This consistency hypothesis underlies the following research question and the focus of this study:

**Research Question:** Will structural forms be consistent among successful firms and distinct from unsuccessful firms, regardless of context and circumstances?

Utilizing an exploratory factor analysis, a technique that facilitates theoretical development in circumstances in which existing theory is unsettled or in which issues remain unresolved (Stevens, 1996), to assess the effects of board composition (Bhagat & Black, 2002; Johnson, Hoskisson & Hitt, 1993; Zahra & Pearce, 1989), equity ownership among directors (Jensen & Meckling, 1976; Hoskisson et al., 1994), and board tenure (Golden & Zajac, 2001; Westphal & Fredrickson, 2001), this study examines two independent samples that capture different types of governance failure and organizational crisis. By examining the factor structures of these three major board control indicators in each setting, we can begin to develop stronger theory regarding the kinds of board characteristics that may successfully correlate with positive firm outcomes in such conditions. The article begins by reviewing the relevant literature on board control, after which the study's methodology and results

are presented and discussed and implications for theory and practice are considered.

## LITERATURE REVIEW

Since Berle and Means' (1932) seminal work, scholars have come to understand that the separation of ownership from management results in an efficient division of labor, but simultaneously presents a control and incentive problem commonly referred to as the "agency problem" (Jensen & Meckling, 1976). Because they cannot diversify their employment capital, managers can be expected to make decisions designed to enhance their employment security or other personal interests (Amihud & Lev, 1981). In order to avoid the negative consequences of such decisions, then, improved monitoring and control of executive behavior must be achieved, and strengthening the board of directors is a critically important means of achieving improved control (Walsh & Seward, 1990). But the board "is not an effective device for decision control unless it limits the decision discretion of individual top managers" (Fama & Jensen, 1983a: 314). Implicitly, this means that the decision management and control functions must be separated, just as ownership and control are separated. The key to the board's ability to monitor and control, then, must be independence from management (Daily & Schwenk, 1996; Johnson, Daily & Ellstrand, 1996). Although boards may be expected to perform a variety of roles (Johnson, Daily & Ellstrand, 1996), it is the function of independent control that remains most important from the standpoint of shareholder protection (Fama & Jensen, 1983a).

As a consequence, the role of the board also has been studied in a variety of contexts, such as restructuring (e.g., Johnson, Hoskisson & Hitt, 1993), takeover defenses (e.g., Davis, 1991; Mahoney et al., 1997; Mallette & Fowler, 1992; Sundarmurthy et al., 1997), and R&D investment (Baysinger, Kosnik & Turk, 1991). Broadly speaking, the research has, consistent with the agency-theoretical perspective, focused on identification of the factors that contribute to board independence and shareholder protection. This study focuses upon three such factors (composition, ownership and tenure) about which some dispute exists or for which inconsistent results have been found.

The proportion of unaffiliated outsiders sitting on the board has received a great deal of attention in both theoretical and empirical research (e.g., Bhagat & Black, 2002; Daily & Schwenk, 1996; Johnson, Daily & Ellstrand, 1996; Johnson, Hoskisson & Hitt, 1993; Zahra

& Pearce, 1989). Outsiders, to the extent lacking direct relationships with managers and the day-to-day operations of the firm, "act as arbiters in disagreements among internal managers and carry out tasks that involve serious agency problems between internal managers and [shareholders]" (Fama & Jensen, 1983a: 315). Despite some empirical evidence supporting the existence of an outsider-performance linkage (Hill & Snell, 1988; Pearce & Zahra, 1992), the general pattern of results found in the literature is mixed at best (Bhagat & Black, 2002; Dalton et al., 1998, 1999; Rhoades, Rechner & Sundaramurthy, 2000). Measurement issues may account for some of this divergence (Daily, Johnson & Dalton, 1999). But another body of research also supports the notion that outsiders, precisely because of their lack of direct involvement with the internal operations of the firm, tend to rely upon financial controls that shift managerial incentives in ways that may not comport with shareholder interests (Baysinger & Hoskisson, 1990; Beekun, Stedham & Young, 1998; Hill & Snell, 1988; Hoskisson et al., 1994). It is also possible that the existence of a reverse causal relationship (i.e., performance causes changes in composition) means that we are not asking the right questions to begin with (Johnson, Daily & Ellstrand, 1996). In short, the precise effects of outside representation are not clear, and certainly do not appear to be universal or monolithic (Deutsch, 2005).

Consistent with agency theory, outside board members' equity ownership also is posited to increase the likelihood that boards will actively monitor the behavior of management (e.g., Hoskisson et al., 1994; Johnson, Hoskisson & Hitt, 1993; Kosnik, 1990). Here, too, the evidence is somewhat mixed. Board involvement in decision-making has been found to be associated with outside director equity ownership (Kosnik, 1990), but Johnson, Hoskisson and Hitt (1993) showed that such directors' ownership was associated with low involvement in refocusing. In the latter case, management itself initiated the action, and while this finding suggests that shareholder interests were realized, it does not fully support the notion of direct control by the board.

Tenure also can be an issue in determining the board's ability to properly constrain management on behalf of shareholders, but again the precise relationship is unclear. In one view, tenure may be associated with rigidity (Boeker, 1997; Finkelstein & Hambrick, 1990; Katz, 1982), while another stream of research suggests that experience arising from long service may be important (Fiske & Taylor, 1991; Hambrick & Mason, 1984). Golden and Zajac (2001) document a curvilinear relationship between board tenure and change, while

Wiersema and Bantel (1992) indicate a positive relationship.

All of these perspectives, of course, emphasize absolute tenure, and the lack of consistency may suggest that the key to the relationship lies in the relative tenure between the board and the CEO. Studies have noted that directors may become, or at least feel, obligated to the CEOs responsible for their appointment (Wade, O'Reilly & Chandratat, 1990; Westphal & Fredrickson, 2001), and therefore CEO power typically is said to increase with CEO tenure (Finkelstein & Hambrick, 1989; Ocasio, 1994). Thus, researchers have begun accounting for the proportion of board members appointed prior to the CEO (Sundaramurthy et al., 1997; Westphal & Fredrickson, 2001) in order to capture the extent of board independence.

With this in mind, attention turns to an elaboration of the study's methodology. Thereafter, the results of the study will be presented and analyzed by looking at patterns that emerge both among successful and unsuccessful firms in both crisis conditions studied here, and by comparing across conditions (successful vs. unsuccessful firm comparisons). In keeping with the research question posed at the outset, if theory is uniform, successful firms in either sample should exhibit the same structures, which also should differ from the consistent structures found among the unsuccessful firms.

## METHODS

The samples for the present study were drawn from firms forced to restate prior-year earnings for reasons other than mere error and those who declared Chapter 11 bankruptcy. The timeframes during which each set of circumstances was prevalent were not identical, and indeed were almost consecutive. Thus, we can gain insight into the board control characteristics that appear to facilitate success (or failure) between conditions and across time. The sample selection and methodological approach applied to each are discussed below.

### Restatement Sample and Data Collection

The tidal wave of financial manipulations that has struck the business world in the past few years provides an opportunity to study governance in action. In examining the role of boards of directors in these circumstances, we can assess the extent to which boards were, or were not, able to avert crisis in the form of managerial wrongdoing and subsequent exposure to scandal. The restatement sample was identified by an electronic word search in Lexis/Nexis Business News for

reports of earnings restatements involving alleged fraud and pending or current legal action by the SEC or private parties. By focusing on reports in which fraud was alleged in connection with the original financial statements, those cases involving presumably deliberate action could be isolated, rather than instances of purely technical restatements. Companies were not included in the sample if such allegations of fraud were unaccompanied by actual restatements. The years between 1996 and 1999, inclusive, were selected as the timeframe for the study, since this period corresponded with generally increasing economic activity and market performance, during which expectations, and performance pressure, were steadily rising.

Following identification of the restating firms, non-restating matching organizations were identified using the primary sample's four-digit SIC code, total assets, and number of employees as matching criteria. This type of design provides de facto control of a variety of inter-firm and extra-organizational influences. Data were matched on the basis of each firm's assets and employees in the year immediately proceeding the primary sample's restatement period. Assets and employees were chosen as match criteria on the assumption that these totals were less likely than earnings to have been subject to manipulation or misstatement. Where more than one possible match existed, the company closest in assets to the restating firm was chosen. After identifying the match and its data availability for the relevant years, a similar word search for the matching firm was undertaken in order to ensure that it had not restated earnings during the sample frame. Matches were identified for all but two of the primary-sample firms, yielding a total sample of 140 companies, comprised of 70 restating firms and 70 non-restating firms. A separate means test indicated that no significant differences on the matching variables existed between the two sets of firms. The same one-year lag procedure for data collection was applied to the non-restating firms, so that full data were gathered for each company, both restating and non-restating, for the year immediately proceeding the restatement year.

### Bankruptcy Sample and Data Collection

The bankruptcy sample is composed of firms experiencing financial distress between 1990 and 1996, inclusive, years during which bankruptcy activity was significant enough to make examination feasible. (Bankruptcies occurring in the years 2000 and following, when bankruptcy activity accelerated again due to the implosion of small, technology-oriented firms, were

excluded from the sample. Such firms tended to file for reasons substantially different than those involved in the earlier timeframe and their internal dynamics, including that of their boards, may well have been distinct enough to skew the final sample and/or mask relationships among the variables had they been included.) The bankrupt firm sample was identified by reviewing the **Bankruptcy Yearbook and Almanac**, an annual publication of New Generation Research that provides a compendium of major bankruptcy developments and filings (Daily, 1996). Companies included in the sample were limited to those filing Chapter 11 reorganizations.

Nonfiling firms were identified using Compact Disclosure and CompuStat as data sources. Each bankrupt firm's total assets, primary three- or four-digit SIC code and debt-to-asset ratio in the filing year was used to identify similarly situated firms with respect to size and industry, and therefore environmental conditions, as well as leverage-related distress. As was true of the restatement sample, where there was more than one possible match, the company closest in assets to the bankrupt firm was chosen. A post-identification validity check revealed that no statistically significant difference in size or leverage existed between the two sets of firms.

In several instances, no valid matches on these measures existed, and accordingly the bankrupt firm was excluded from the sample. However, where matches were identified, the matching firm was cross-checked against the **Bankruptcy Almanac's** lists of bankruptcies in both preceding and subsequent years to ensure that the match was not itself either a reorganized firm currently operating outside of bankruptcy or a firm that entered bankruptcy within three years of the sample window. Where such was the case, the prospective match was excluded and a new match was sought. This procedure resulted in a total sample of 220 firms, comprised of 110 bankrupt firms and 110 nonbankrupt firms.

### Measurement of Board Control Characteristics

Common measures of board control reflecting the constructs discussed above were calculated for both samples. Outside director percentage was calculated as the ratio of unaffiliated outsiders (i.e., those with no past or current personal or professional relationships with the focal organization) to total board members (Hoskisson et al., 1994; Johnson, Hoskisson & Hitt, 1993). Outside director equity ownership was calculated by dividing the shares owned by such outside directors by total shares outstanding (e.g., Hoskisson et al., 1994; Johnson, Daily

& Ellstrand, 1996). Consistent with the perspectives elaborated above, measures of absolute and relative tenure were calculated. Average board tenure (total years of experience divided by board size) and average outside director tenure (total years of outside director experience divided by number of outsiders) were the measures of absolute tenure used in the study (e.g., Golden & Zajac, 2001). Relative tenure was calculated both as the percentage of directors appointed prior to the current CEO (Sundaramurthy et al., 1997; Westphal & Fredrickson, 2001) and as the average tenure of the board divided by the tenure of the CEO (Daily & Schwenk, 1996; Johnson et al., 1996).

### Analytical Method

Based on the foregoing variables, we conducted an exploratory factor analysis based on principal components, a technique designed to identify a series of uncorrelated (between factors) linear combinations accounting for the maximum possible variance in the focal variables. Unlike confirmatory analysis, principal components analysis does not specify an *ex ante* factor structure; rather, all variable loadings and the resultant identifiable factors are determined purely by the variable values themselves. In this sense, the approach is exploratory, and the object is to assess variable combinations and factor structures in situations in which theory is unsettled or undeveloped (Stevens, 1996).

In performing the analysis, factors with eigenvalues greater than one after Varimax rotation (Kaiser, 1960) were retained. Individual factor loadings, representing the correlations between the factor and the variable, were considered significant if they were equal to or greater than twice the critical value for correlation significance at the .01 level (Stevens, 1996).

For the restatement sample, this cutoff (double the standard correlation coefficient) is approximately .43, and approximately .35 for the slightly larger bankruptcy sample. Finally, Bartlett's test of sphericity (Cooley & Lohnes, 1971), which assesses correlation among the population variables, was conducted as an additional validity check.

### Results

Tables 1 and 2 present the correlation matrices for the restatement and bankruptcy samples, respectively. An examination of these tables reveals interesting correlations between absolute tenure and restatement activity (negative) and between relative tenure and bankruptcy (positive). These issues are discussed in

greater detail below in conjunction with the results of the factor analyses. In passing, note that intra-factor variable correlations are not a necessity for the existence of viable

factors (Nunnally, 1978), for the factor loadings in essence represent correlations between the variable(s) and the latent construct (Stevens, 1996).

**Table 1: Correlations and Descriptive Statistics (Restatement Sample)**

Variable	Mean	S.D.	1	2	3	4	5	6	7
1. Restatement <sup>‡</sup>	.50	.50	1.000						
2. Outside director percentage	.60	.21	.069	1.000					
3. Outside director ownership	.05	.09	.021	.039	1.000				
4. Average tenure	7.39	5.18	-.308***	-.110	-.162*	1.000			
5. Outside director tenure	5.23	4.49	-.254**	.239**	.002	.741***	1.000		
6. Pct. appointed before CEO	.39	.33	-.132	-.048	.146†	.204*	.268***	1.000	
7. Board-to-CEO tenure	1.81	2.32	-.081	-.109	.016	.249**	.186*	.611***	1.000

N=140. ‡ = Coded 0 (no) or 1 (yes).

† p < .10, \* p < .05, \*\* p < .01, \*\*\* p < .001.

**Table 2: Correlations and Descriptive Statistics (Bankruptcy Sample)**

Variable	Mean	S.D.	1	2	3	4	5	6	7
1. File <sup>‡</sup>	.50	.50	1.000						
2. Outside director percentage	.56	.20	.011	1.000					
3. Outside director ownership	.04	.13	-.107	-.004	1.000				
4. Average tenure	8.05	5.01	.019	-.161*	-.061	1.000			
5. Outside director tenure	6.49	4.77	.028	.081	-.108	.775***	1.000		
6. Pct. appointed before CEO	.21	.21	.146*	.086	.098	-.051	-.080	1.000	
7. Board-to-CEO tenure	1.41	2.13	.263***	.022	-.051	.123†	.316***	.303***	1.000

N=220. ‡ = Coded 0 (no) or 1 (yes).

† p < .10, \* p < .05, \*\* p < .01, \*\*\* p < .001.

**Table 3: Results of Principal Components Analyses**

Variable	Bankruptcy Sample				Restatement Sample		
	Factor 1	Factor 2	Factor 3	Factor 4	Factor 1	Factor 2	Factor 3
<i>Unsuccessful firms:</i>							
Outside director percentage	.037	.005	-.010	.993	.107	-.549	.065
Outside director ownership	.042	.017	.974	-.013	-.077	-.001	.977
Average tenure	.891	-.104	.137	-.096	.895	.172	-.165
Outside director tenure	.912	.126	-.048	.187	.960	-.077	.058
Percentage appointed before CEO	-.075	.915	.092	.044	.188	.798	.203
Board-to-CEO tenure	.518	.577	-.251	-.099	.098	.863	-.083
Eigenvalue	1.991	1.145	1.040	1.006	2.017	1.514	1.009
Percentage of variance	.332	.191	.173	.168	.336	.252	.168
<i>Successful firms:</i>							
Outside director percentage	-.278	.358	-.642		.148	-.119	.897
Outside director ownership	-.243	.259	.759		-.261	.444	.522
Average tenure	.954	-.127	.079		.893	.145	-.192
Outside director tenure	.932	.149	-.119		.885	.176	.324
Percentage appointed before CEO	.040	.874	.105		.145	.862	.072
Board-to-CEO tenure	-.015	.880	-.087		.203	.830	-.093
Eigenvalue	1.988	1.706	1.022		2.190	1.280	1.191
Percentage of variance	.331	.284	.170		.365	.213	.199

Table 3 shows the results of the principal component analyses of the two samples, in each case showing the comparison between the unsuccessful firms (those experiencing the event) and their matches (those avoiding the event). Beginning with the restatement sample, table 3 reflects the existence of three factors for both the restating and non-restating firms, but with divergent factor loadings. The non-restating firms exhibit a relative tenure/ownership factor (high loadings for percentage

appointed prior to the CEO and board-to-CEO tenure combined with a moderate level of ownership at .44) that is distinct from an absolute tenure factor (outside tenure, .885; average tenure, .893). The third factor combines ownership (.522) with outside representation (.897).

The pattern of loadings differs for the restating firms. Although a similar absolute tenure factor exists (outside tenure, .960; average tenure, .895), ownership and relative tenure exhibit different effects. Unlike the co-

loading found with respect to ownership among the non-restating firms, among restaters ownership represents a single-item factor (.977). Relative tenure is bipolar, with high positive loadings for percentage appointed prior to the CEO (.798) and board-to-CEO tenure (.863) and a negative loading for outside representation (-.549). This suggests a pattern of high relative tenure on boards with minimal outside presence.  $N=220$  for Bankruptcy Sample, 140 for Restatement Sample. Factors retained if eigenvalue  $> 1$ . Values represent factor loadings after Varimax rotation. Loadings significant at 2 x correlation significance critical value ( $p < .01$ ) in bold.

## DISCUSSION

This paper began by asking the question whether, in light of recent events, we can conclude that our existing theoretical framework regarding board control is complete or applicable in all circumstances. Despite considerable attention to the role and importance of boards in controlling management (Fama & Jensen, 1983a), boards seemingly failed to exercise appropriate oversight in many companies. Yet it is not precisely clear what differences, if any, existed in the control regimens of either "good" or "bad" firms, and our theories would seem to suggest that a uniform distinction can and should be drawn between such companies based on observation of certain structural forms. Such was the implication of the consistency hypothesis with which the article began.

The objective of this study was to incorporate a variety of board control characteristics within an exploratory analytical approach that would permit us to assess differential control patterns contributing to successful avoidance of crisis. Broadly speaking, as can be seen in table 3, the results of this analysis suggest that different control patterns emerge both within and between each of the two crisis contexts examined. Post hoc MANOVA and regression analyses confirmed differences existed particularly with respect to tenure, with the restatement sample exhibiting primary effects for absolute tenure and relative tenure exerting the greatest influence in the bankruptcy sample. This suggests that the answer to the research question upon which this study focused is negative, and that the consistency hypothesis is not supported. As discussed below, it is also possible discern situations in which adherence to the form of good governance was inadequate to prevent the onset of crisis. Indeed, it may be that such firms engaged in a certain amount of window-dressing behavior - or, possibly, they believed the steps they were taking, in themselves consistent with

normative standards of governance, would successfully help them avert future difficulties. Unfortunately, such was not the case.

Beginning with the factor patterns observed among successful firms and among the unsuccessful companies, table 3 shows that more similarity exists among the former than the latter, but that differences also exist even here. In both contexts (bankruptcy and restatement activity), the firms able to avoid crisis exhibited a clear board tenure factor, both in absolute and relative terms. As noted earlier, the literature is split with regard to the effects of tenure, but one stream (e.g., Fiske & Taylor, 1991; Golden & Zajac, 2001; Hambrick & Mason, 1984) supports a knowledge perspective in explaining why, in certain circumstances at least, tenure may be beneficial. Specifically, tenure facilitates the gathering of information and the development of perspective concerning the organization that may contribute to success. Board stability, for example, has been found to be associated with positive outcomes in other contexts (Crutchley, Garner & Marshall, 2002). These findings are supported by the results observed here.

There are, however, interesting and important distinctions between the two samples as far as outside director influence is concerned. In the restatement sample, successful firms combine relative tenure (Daily & Schwenk, 1996; Sundaramurthy et al., 1997; Johnson et al., 1996; Westphal & Fredrickson, 2001) with outside director ownership. Thus, director independence based upon tenure relative to that of the CEO is supplemented by actual authority as shareholders, and by the incentive alignment properties asserted on behalf of equity ownership (Jensen & Meckling, 1976). Similarly, the non-bankrupt firms combined relative tenure with high outside director percentages. In other words, these firms relied more upon long-serving outsiders without ownership interests in the firm. The key message seems to be that successful firms coupled some form of outside director participation with tenure, which would seem to suggest that governance failure can be avoided with the proper combination of independence and interest.

The major distinction between the two crisis contexts, apart from the form of outside participation combined with relative tenure, resides in the outside director factors observed in each case. That is, in the restatement sample, successful firms had both high levels of outsiders and high levels of outside director ownership, while in the bankruptcy sample, successful firms apparently relied upon a few outsiders with significant ownership stakes and other outsiders with long tenure. Gilson (1989, 1990) documented the tendency of outside directors (and

management) to depart from failing firms and for ownership to become concentrated, and the factor loadings observed in this instance are broadly consistent with his findings. Indeed, these owner-directors may represent significant owners seeking a voice on the board to protect and oversee their investments, which may reflect the traditional view of incentive alignment via equity ownership (Jensen & Meckling, 1976). The distinction between this case and that of the restatement sample firms suggests the existence of a contingency for which theory must account.

By contrast, the unsuccessful firms exhibited less commonality in their factor patterns. Only a common, single-variable ownership factor is shared among these firms, with all others showing some variation between the two different crisis conditions. But note that in this respect ownership alone was not sufficient to forestall crisis. The unsuccessful firms thus may have been seeking the form of good governance without adopting other practices that might ensure success. The same general tendency can be noted among the bankrupt firms, who also exhibited a separate outside director factor that was uncombined with ownership or any of the other variables. Baysinger and Hoskisson (1990) argued that some insiders are necessary to provide rich perspective. Given this, it may be that the bankrupt firms sought the legitimacy of high outside representation at the expense of analytical depth and clear understanding of the operational functions of the organization.

Examining the pattern of factors between the two crisis conditions reveals important implications for tenure, ownership and outside involvement. Note first that similar board tenure loadings across conditions exist for the restatement sample, but not for the bankruptcy sample. In the latter case, relative tenure (board-CEO tenure ratio) loads with the absolute tenure variables. Thus, unlike the companies in the restatement sample, the bankrupt firms' boards combine both high levels of absolute tenure with higher levels of tenure compared to that of the CEO, suggesting CEO turnover. This, of course, is not an uncommon occurrence among distressed firms (Daily, 1996), and may suggest that, far from becoming inhibited by a threat-rigidity response (Staw, Sandelands, & Dutton, 1981), these firms may have undertaken too much change for their own good. When managing crisis, in other words, too much turnover among management teams and boards may interrupt knowledge development and application that could benefit the firm and contribute to survival. However, the similarity in tenure loadings in the restatement sample between the successful and unsuccessful firms gives

some pause to conclusively finding for board tenure as a preferred governance mechanism. The post hoc analyses alluded to above disclose the existence of different tenure effects between the two crisis conditions that provide additional gloss on these observations: relative tenure had the greatest influence in the bankruptcy sample while absolute tenure was predominant in the restatement sample. The latter may suggest a power or authority interpretation, while the former may invoke an issue of resources, particularly given the apparent simultaneous emphasis on outsiders (e.g., Daily, 1996). Additional theoretical development of these relationships clearly is necessary.

Likewise, comparing results for ownership and outside representation across the samples confirms and extends the conclusions drawn from analysis of the successful and unsuccessful firms alone. Specifically, successful firms tended to combine ownership or outside representation with something else, whereas the unsuccessful firms either lacked one of these attributes (restating firms with low outsider percentages) or retained them independently. This implies that, despite the putative benefits of incentive alignment arising from equity ownership (Jensen & Meckling, 1976), ownership does not appear to improve governance individually; it must supplement other characteristics to be effective. Therefore, in promoting outside director equity, we may have sought to advance the project of governance reform too far, at least to the extent ownership was viewed as a sufficient source of effective control. Similarly, reliance upon outside directors alone was a common feature of the unsuccessful firms that confirms some theory (Baysinger & Hoskisson, 1990) advocating a balance of perspectives. The results here thus highlight the need to develop firm- and context-specific governance solutions.

## CONCLUSION

Theory has advanced the notion that certain governance forms and structures can be relied upon to work, and many such rules-based solutions have carried forward into the current reform movement. Certainly, much has been made of the need for, among other things, independent, outside directors with appropriate compensation systems that bind their interests to those of shareholders. One firm stands out as an exemplar of this model: Enron (Kocourek, Burger & Birchard, 2003; Kulik, 2005). Although with hindsight we might question the extent to which the Enron directors were truly independent, at the time the company's overall governance seemed consistent with general practice.

What, then, went wrong? The answer seems to lie in a tendency to rely upon form and adherence to generalized norms, rather than to conduct the kind of firm-specific analysis that might yield better results. Indeed, the findings of this study suggest that our theoretical understanding of board control should be augmented and adjusted to reflect the circumstances present in individual cases. This represents a significant challenge for both practitioners and academics, for the stakes are large. But understanding that general rules may not be applicable to all contexts is itself an important first step in designing appropriate governance systems, and this is one of the primary contributions of this research. In addition, the study highlights some of the areas that may hold promise for future research and practice, including the effects of tenure, especially as it may be decomposed into different aspects in different circumstances, and the apparent ineffectiveness of board equity ownership. Reliance upon ownership alone, for example, was not a characteristic shared by the successful firms studied here. Instead, a combination of approaches seemed to be developed that in themselves differed by context. And context, rather than rules of thumb, clearly must be the basis of our solutions.

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