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Headaches, Concerns, and Regrets: What Does the Experience of 102 Brazilian Directors Tell Us?

Sandra Guerra and Rafael Liza Santos

This paper takes a look inside the functioning of the modern corporate board “black box.” Using results of an anonymous online survey, it investigates the experiences and behavior of 102 Brazilian directors—from an individual perspective as well as from a group one. To gain insight into what goes on in directors’ minds, the authors adopted a behavioral approach based on extensive literature regarding cognitive biases and group dynamics.

Foreword

In my work with boards and interactions with practitioners and policymakers, I have been keen to emphasize the transition of focus in board governance from structures and processes to group dynamics and individual director behavior. There is growing recognition in many markets that the requisite board “hardware” is generally in place at large listed companies (although not always implemented effectively) and that it is now vital to improve its “software” to enable these bodies to perform to their potential.

Veteran banking expert David Walker, in his examination of corporate governance shortcomings at financial institutions in the run-up to the global financial crisis, observed that the “principal deficiencies in [bank] boards related much more to patterns of behavior than to organization.” Recently, the U.K. Financial Reporting Council began homing in on the behavioral aspects of board functioning, warning—for example—that a “dominant personality or group of directors on the board can inhibit contribution from other directors.”

In my different capacities, I have come across problematic boardroom dynamics and behavior, such as a chairman who was persistently overshadowed by a “star” chief executive officer, outside directors who relished playing “gotcha” with management by repeatedly pointing out their missteps, and a board that allowed the allure of complex quantitative models to dull the critical faculties and common sense of its members.

In this vein, it has been delightful to review Sandra Guerra's and Rafael Liza Santos's Private Sector Opinion. Their pioneering effort to open the boardroom black box and peer into the minds of Brazilian directors has yielded a number of fascinating insights. It is my hope that their work will lead to further exploration—by the authors and others—of this and related areas in an effort to expand the empirical fact base, strengthen statistical robustness, and deepen our collective understanding.

With regard to their findings, it is remarkable that cognitive biases are so pervasive in Brazilian boardrooms. According to the authors, 74 percent of the survey respondents mentioned herd behavior as a frequent or very frequent occurrence in board decision making, and nearly two-thirds cited groupthink as a common malaise. It would be interesting to see whether these biases plague boardrooms in other countries to the same (or even greater) extent.

Directors I have spoken with over the years acknowledge—although they may be reticent to state it publicly—stylistic differences between men and women that affect, among other things, the character of board discussion, the way feedback is delivered and received, and the collegial nature of the board itself. Guerra's and Santos's research has found that gender differences extend to the willingness to express regrets, with men less comfortable admitting mistakes and perhaps also suffering from overconfidence. In my view, exploring ways to encourage honest introspection on the part of individual directors and the collective board would help improve the quality of its work by enhancing its ability to take early corrective action and avoid the recurrence of errors.

All over the world, boards have performed inadequately on succession planning, often tackling it too late or allowing the incumbent chief executive officer to be overly influential. While some may focus on the finding that one-third of the survey respondents had regrets about the way their company's chief executive was selected, I was surprised that two-thirds felt that their companies had adopted the right approach on chief executive officer succession. It would be a great service to boards everywhere to gain a better understanding of what these boards had done right.

The differences in views between independent and non-independent directors are also intriguing. The authors provide further support for the value of independent directors in the boardroom, who—the survey revealed—exhibited a stronger awareness of conflicts of interest. At the same time, it surprised me to learn that non-independent directors were more concerned about poor corporate governance practices and inadequate risk management than their independent peers.

This Private Sector Opinion by Sandra Guerra and Rafael Liza Santos contains many illuminating insights, and I believe that board members, corporate management, and others with an interest in corporate governance will find it a worthwhile read.

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Headaches, Concerns, and Regrets: What Does the Experience of 102 Brazilian Directors Tell Us?

Sandra Guerra and Rafael Liza Santos¹

Boards of directors are among the most secretive, obscure, and influential corporate entities in modern capitalism. Very few people in the business world ever have the opportunity to actually see how board meetings are conducted and how directors interact. Nonetheless, corporate finance literature indicates that boards and the decisions they make play a crucial role in the performance of companies.²

This paper aims to take a closer look inside this so-called “black box.” Specifically, we investigated the experiences and behavior of 102 Brazilian directors, from an individual as well as a group perspective. Using a questionnaire, we conducted an online survey that guaranteed anonymity to the participants.³ We asked questions about their profile, board seats, experiences, concerns, and regrets. To understand what goes on in directors’ minds, we adopted a behavioral approach based on extensive literature regarding cognitive biases and group dynamics. Our results identify the hardest decisions that directors face in the course of their work, how their so-called level of independence affects their perception of difficulty on any given subject, and how gender is linked to their regrets in connection with a certain “wrong” decision they feel that they made. Our survey also sheds some light on what directors would have done differently had they known at the time what the results of their decisions would be. Overall, this article provides a pioneering insight into the work and inner workings of boards of directors—from the insider’s point of view.

A Black Box

The board of directors operates like a closed black box. Boards are very complex social structures that have to perform extremely difficult duties. It is getting tougher and tougher to be an effective director. The pace of change in today’s world is, in its own way, forcing every business to become global and is constantly making the business world less secure. Boards have to deal with disruptions that are changing the face of businesses in just a couple of years. As a consequence, it is not surprising that some boards are failing to perform their tasks properly.

The board of directors operates like a closed black box.

¹ Sandra Guerra has more than 21 years of experience in corporate governance as well as an extensive career as a c-level executive and board member in multiple companies. She was a co-founder and chair of the Brazilian Institute for Corporate Governance and a board governor of the International Corporate Governance Network. Sandra holds a master of science degree in business and is an accredited mediator at the Centre for Effective Dispute Resolution in London.

Rafael Liza Santos has 10 years of experience as a management consultant in corporate governance, business strategy, and corporate finance. His research on corporate governance has been published in local and international journals. Rafael holds a degree in economics from the University of São Paulo and has completed specialized study in applied economics at the University Paris-Dauphine in France.

The authors wish to thank Alessandra Polastrini who was key in preparing and reviewing the charts presented in this paper.

² Prior research has suggested that there is a direct relationship between board performance and the resulting corporate financial performance and that companies with active boards produce higher levels of investor returns and economic value creation than those with passive boards, but this has not yet been proven by means of empirical research (Charas 2015).

³ Directors answered the survey questionnaire between May 2015 and January 2016.

Sir Adrian Cadbury,⁴ who was a leading expert on corporate governance, pointed out that boards are failing to prevent corporate scandals. After all, despite tremendous efforts in the 1980s and 1990s to establish and strengthen corporate governance regulations, boards were still failing in 2001 and beyond. In Cadbury's opinion, directors are not asking the right questions, they are not monitoring chief executive officers adequately, and they are failing to support executives in defining strategy guidelines and corporate purposes. This scenario is fertile ground for corporate governance issues to arise and grow.

Over the last 50 years, research into the performance of boards of directors has focused on individual directors' economically motivated behaviors and outcomes, and it has generated inconsistent and disappointing results. Most research does not consider the board as a team, despite recent calls for a focus on collective board processes and behaviors (Charas 2015; Forbes and Milliken 1999). To better understand board performance, it is important to be aware of how directors interact with each other and how they actually make decisions. Morten Huse (2005) suggests that analyzing boards' composition, processes, working style, and internal dynamics may well provide a more solid conclusion. Therefore, understanding boards requires a new approach that focuses on the reasons for the destructive board dynamics that have undermined the abilities of well-intentioned board members to provide good corporate oversight.

Recent studies⁵ show that the limits of rationality, information asymmetry, and cognitive biases provoke a sort of "blindness" that prevents directors from making the proper decisions.

“. . . [I]deal boards, those with 'best practice' size, composition, and structure, with enough staff support, and with enough time to consider issues carefully, can still fail to provide good governance, simply because they fall victim to some problems inherent in all groups. That is, all groups of individuals who are trying to work together for the common good are subject to some destructive group dynamics that cause blind spots, biases, and other decision-making pathologies. Recognizing these problems is a first necessary step. Only then can steps be taken to avoid the problems, or at least to minimize their consequences” (Pick and Merchant 2010).

Some researchers believe that, in addition to all the rules, practices, mechanisms, and processes adopted by a board, there are factors that are not yet on the radar of most boards: the behavioral dimensions—from individual or group perspectives (Pick and Merchant 2010; Forbes and Milliken 1999). Perhaps the reason the behavioral dimension was outside the main focus was because companies and business leaders were working under the classical assumption that people are rational and that consequently their decisions—particularly in business environments—are essentially rational. This assumption of classical economics theory prevailed for a long time before modern concepts of psychology and sociology came forth to challenge it.

Studying how directors make decisions and what role their limited rationality plays in the performance of firms is one of the most relevant challenges facing corporate governance studies today

⁴ Sir Adrian Cadbury authored the Cadbury Report, published in 1992, which helped define corporate governance standards all over the world, and was chairman of Cadbury Schweppes board. Before his death on September 3, 2015, at the age of 86, he gave an interview to Sandra Guerra at his residence in Dorridge, in the United Kingdom. That December 4, 2013, interview is the source of comments referenced here.

⁵ For example, Nutt 1986; Jackson, Stone, and Alvarez 1992; Pearce and Zahra 1992; Zald 1969; Pfeffer 1972, 1973; Pfeffer and Salancik 1978.

Herbert Simon, who won the 1978 Nobel Prize in Economics for his pioneering research into decision making within economic organizations, argued that it is impossible for the behavior of a single, isolated individual to reach any high degree of rationality. Simon concludes that human behavior is intentionally rational but only limitedly so.

The concept of bounded rationality opens up a whole new perspective, recognizing human limits in the processing of information and the consequent inability of managers to make optimal decisions in an economically rational manner. However, assessing the behavioral dynamics of an individual or a group is an extremely difficult task. Most of these cognitive biases are unperceived by us, and we can see nothing but their effects on the outcomes of decisions we make. For this reason, studying how directors make decisions and what role their limited rationality plays in the performance of firms is one of the most relevant challenges facing corporate governance studies today.

This study aims to contribute to the understanding of this aspect of decision making by investigating individual and group attitudes and behaviors in a board setting. For example, how frequently do directors recognize cognitive biases? And it puts these data into the context of multiple characteristics of board members, such as background, major concerns, and regrets.

Inside the Box: What Directors Actually Do

Our sample broadly reflects the characteristics of the average board member in Brazil. More than 83 percent of the directors who answered the questionnaire are male, almost half (46 percent) are 60 years old or older, and 55 percent have been serving on boards for the last 10 years. The 102 directors who answered this questionnaire average more than 11 years of board experience, and at least 30 percent have spent most of their professional life on the boards of publicly listed companies.

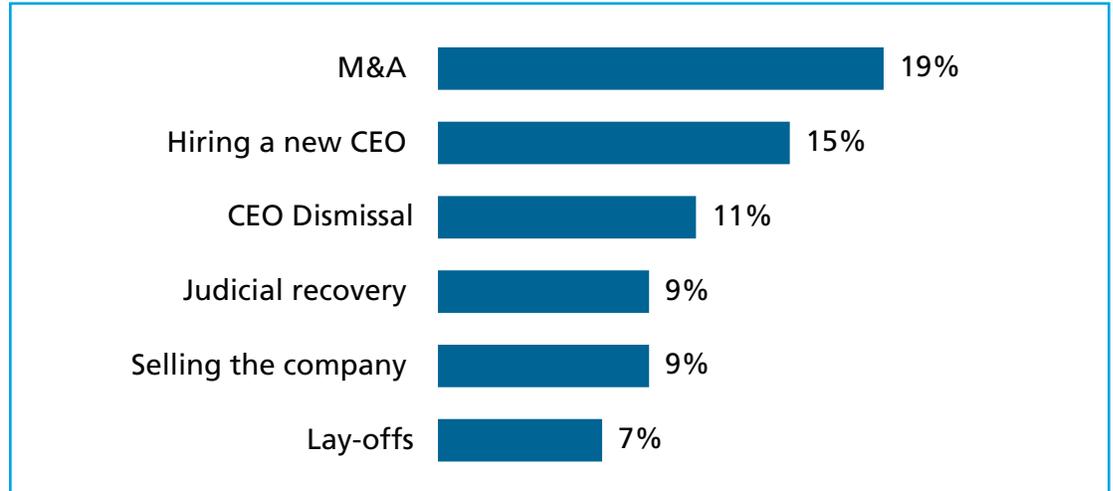
We should note that the participants in our survey were contacted through the personal and professional network of one of the authors of this report. Therefore, that author's expertise in the field of corporate governance and her efforts to promote good practices may have weighted the survey toward directors who were already inclined to have a higher commitment to good corporate governance practices, causing a certain bias in their answers.

In Brazil, as in most emerging markets, there is a high concentration of ownership among a few shareholders. Therefore, 48 percent of the directors in our sample have served on the boards of privately held firms where there is a clear controlling block. More than half of them have served as an independent board member, according to their self-declaration. Unfortunately, we cannot ensure actual independence, given that they were elected by controlling shareholders.

Hardest Decisions and Regrets

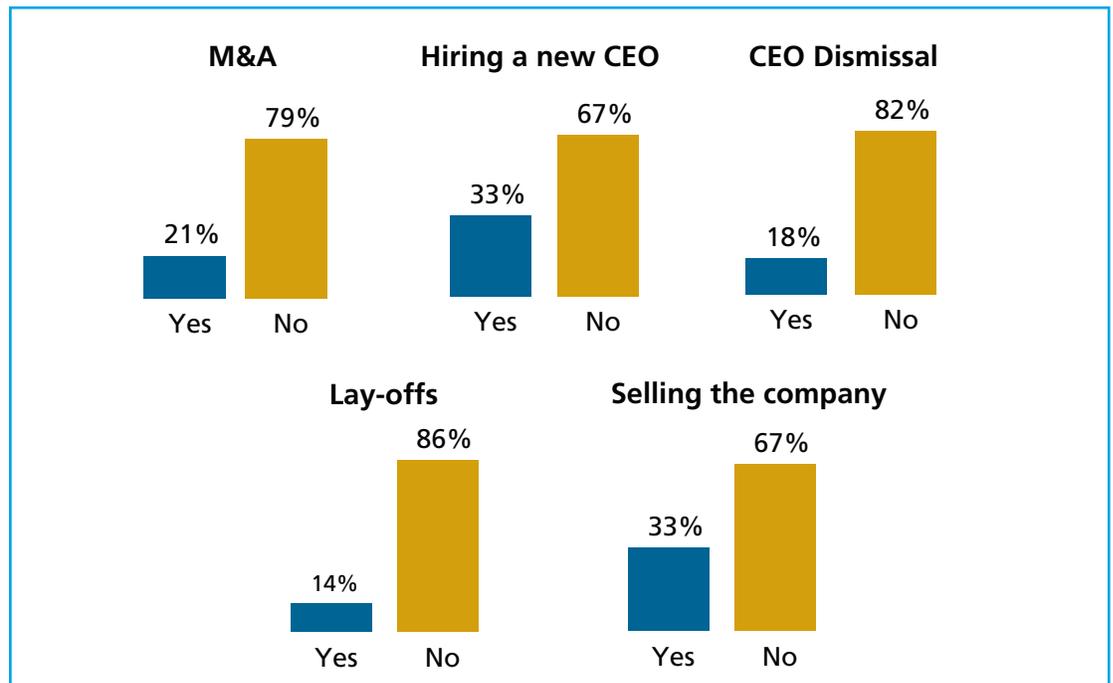
The questionnaire asked, “What was the most difficult decision you have taken in your time as a board director?” Figure 1 shows the top six responses, accounting for 70 percent of the total number of answers from a list of 15 alternatives. Note that hiring a new chief executive officer and dismissing one, combined, gathered more than a quarter of the votes.

Figure 1: Hardest Decisions as Board Members



Sometimes the results of director’s decisions are not exactly what they expected. We looked into this further and asked directors, “About this decision, would you have taken a different approach now that you know the results and consequences?” Almost a quarter of all directors (24 percent) responded positively. Figure 2 shows the top five answers from the 15 alternatives. It is notable that a third of all respondents (33 percent) would have done something differently in hiring a new chief executive officer and in selling the company, by far the largest number of “yes” responses.

Figure 2: Top Five Decisions and Directors’ Regrets



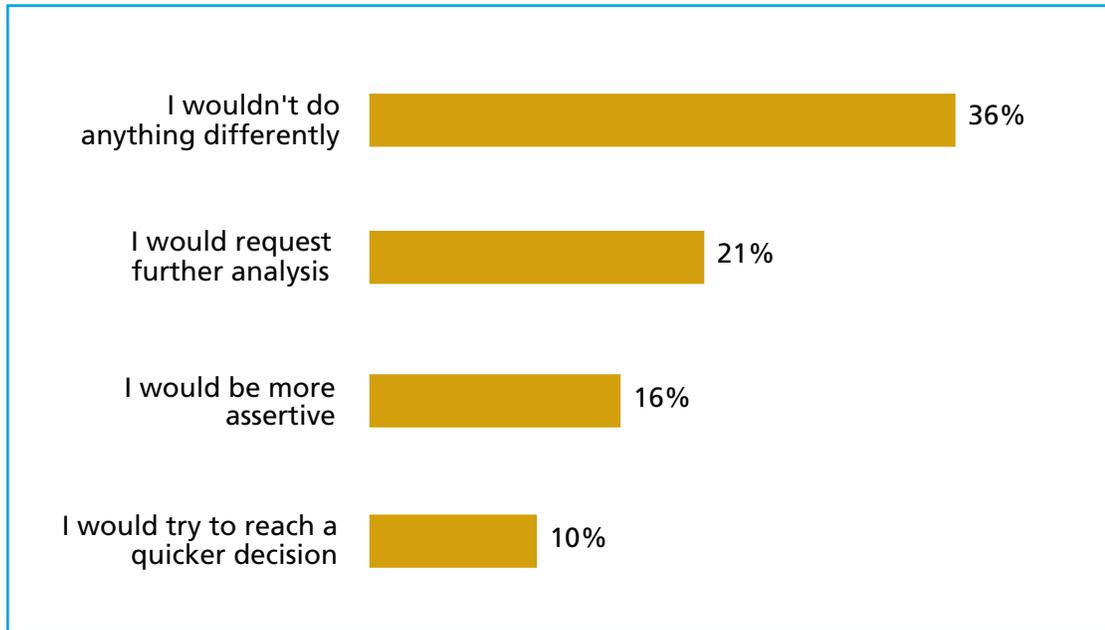
We asked, “About this decision, what would you have done differently now that you know the results and implications?” We found it interesting that 36 percent of the directors said they wouldn’t do anything differently regarding their hardest decisions. This indicates that, though the decision was considered hard in hindsight, they believe they made the right call and don’t regret it.

Of the 64 percent who would have done something differently, the most common reason mentioned (21 percent) was the lack of sufficient analysis. Decisions on the board are often presented as *urgent or very urgent*: “The opportunity window will close, so we need to reach a decision quickly.” “The buyer will only wait until next week for our offer.” In the face of tight time constraints and uncertainty, directors may be subject to cognitive biases, such as herd behavior—following the opinions of others who previously stated their personal views. This may lead to bad decisions on the part of the board.

At the same time, 10 percent of the directors said they would have reached the decision more quickly, indicating that the speed of the board decision is indeed sometimes an important component of the quality of the outcome. Distinguishing between truly urgent decisions and those that need further analysis is one of the challenges a board director faces. Figure 3 shows the top four categories of responses to the question, accounting for 83 percent of the total answers.

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Figure 3: Hardest Decisions: Adoption of a Different Approach



Regrets: women are more prone to admit that they would do things differently. Once they are aware of the impact of their decisions, female directors are more prone to assume that they would have taken a different approach. While only 16 percent of male directors answered that they would do something differently regarding a past decision, the number is more than double (39 percent) for female directors. Although we do not have the means to test the reasons for this discrepancy, we can speculate that 1) women may be more comfortable admitting their mistakes, and 2) men more frequently exhibit overconfidence and excessive optimism, which can cause them to think they have made the right decisions even though this might not be true.

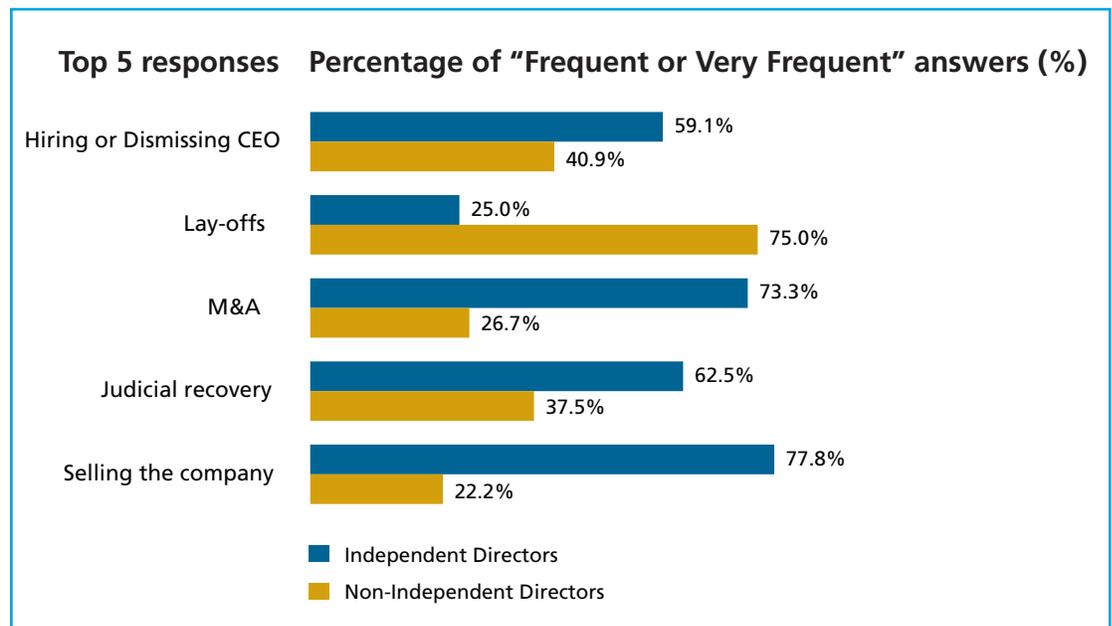
Decisions: some decisions are harder for independent directors. A director's independence may affect how he or she sees a set of alternative solutions to a particular problem. In Brazil, the norm is for ownership to be concentrated. Usually, controlling shareholders are able to own a large stake in the company or create shareholders' agreements in which they hold controlling blocks. For this reason, those major shareholders are able to elect their own

directors or at least have a high degree of influence over the election of the board, even if the company is a publicly listed one, due to the low level of free float in the market. When directors are somehow linked to the controlling shareholders, either because the shareholders elect them or because they feel they should act as representatives of the controlling block, they may face a conflict of interest when taking decisions for the company.

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Since this link to a certain group of shareholders may interfere in their decisions, we separated the two groups of directors, based on their self-declared level of independence, when considering their answers to the question, "What was the most difficult decision you have taken in your life as a board director?" Figure 4 shows the percentage of combined "frequent" and "very frequent" responses to the top five areas of decision making from self-declared independent and non-independent directors.

Figure 4: Hardest Decisions: Variations Based on Directors' Self-Declared Independence

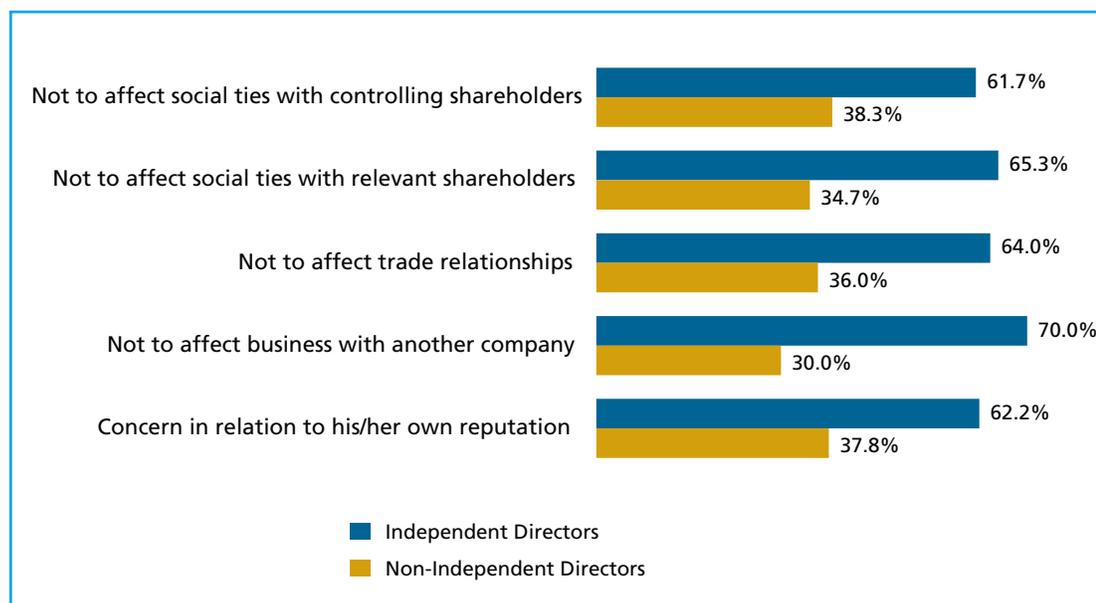


Independent directors tended to find the questions about most of the issues listed in Figure 4 more difficult than non-independent directors did. The exception was the issue of layoffs, which non-independent directors found more difficult. The reason for this exception is beyond the scope of our survey, but it may be linked to the non-independent directors' greater involvement in the firm's operations (as executive directors) and the consequences of their decisions regarding layoffs.

Independence and Conflicts of Interest

The independent directors also seem to be more alert to the actual or perceived conflicts of interest in board decisions. The questionnaire asked, "In certain situations, do you ask yourself if the other director's motivation is really the best alternative for the company or if he or she has another reason that is directing his or her behavior? What were the most frequent causes that prevented them from acting in the best interests of the company?" Figure 5 shows the percentage of answers for self-declared independent and non-independent directors and indicates that independent directors have a higher degree of perception regarding the reasons directors sometimes may not act in the company's best interests.

Figure 5: Reasons for Not Acting in the Company's Best Interest—Based on Self-Declared Independence



Independence also affects how directors see the reasons for their own mistakes. Asked to "choose up to three causes related to your performance that you consider a mistake nowadays," significantly more independent than non-independent directors indicated that they were "influenced by others who intentionally underestimated risks and costs" (14 percent versus 7 percent) or "did not investigate the source of the information" (8 percent versus 2 percent). Both causes speak to the well-known information asymmetry between independent and other directors, especially executive directors.

At the same time, the non-independent directors indicated that they were more often "influenced by a previously declared decision of other directors" (10 percent versus 6 percent of independent directors).

Beyond Box Ticking: Behavioral Approach to Boards

Fundamentally, board performance depends on how directors interact with each other and how they get along with the executives. Pick and Merchant (2010) indicate that some aspects of directors' interactions can jeopardize the talents of intelligent and well-intentioned people, causing blind spots, biases, and inefficiencies that can lead to boards becoming ineffective. In some cases, cognitive biases can cause highly qualified boards to ignore risks and problems that they would otherwise easily perceive. Also according to these researchers, boards sometimes make decisions that none of their individual participants would make alone.

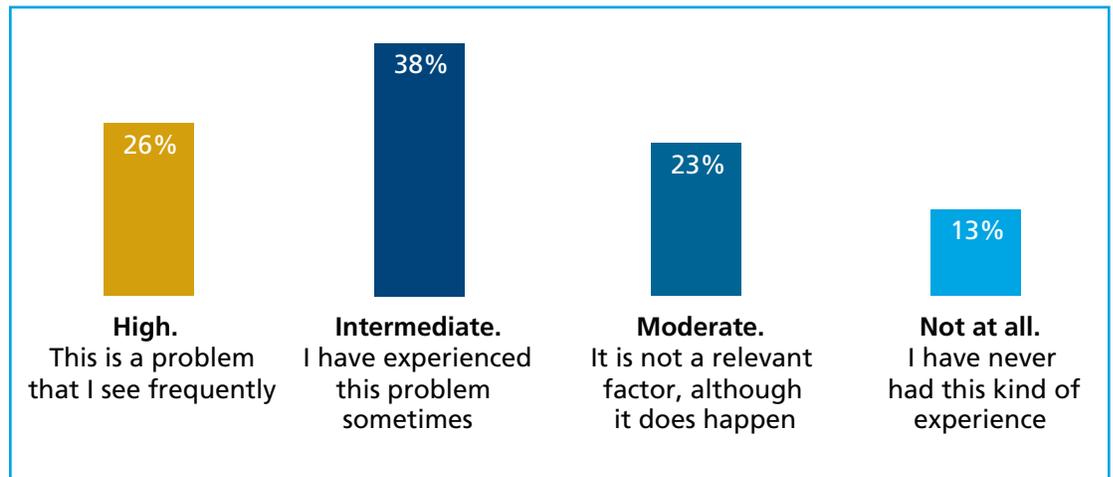
But what are those “cognitive biases,” and how do they affect our thoughts? Cognitive biases are mental behaviors that poison the decision-making process. They can occur at the individual as well as the group level.

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Some cognitive biases have to do with the way the information is presented to someone. For instance, we tend to prefer a product that's described as “90 percent fat free” instead of as “contains 10 percent fat,” even though both statements are essentially the same. This common form of presentation bias is known as “framing.” A framing bias occurs when the way or order in which a piece of information is presented affects our opinion about it. At a board meeting, when a certain director is the first one to state his or her opinion, this might affect (or frame) the other members' opinions as well, therefore creating a bias toward the view presented.

Our questionnaire asked, “Some decision-making processes begin with previously formed perceptions and beliefs, which almost never disappear, even though there's no empirical evidence supporting them. How relevant was this phenomenon in your life as a board member?” Figure 6 breaks down the responses.

Figure 6: Biases Regarding Previously Formed Beliefs and Opinions



Within boardrooms, individual biases seldom occur in isolation. When people are grouped together, biases can be intensified and may expand to become group biases. The dynamics of the group can become more complex or, eventually, even ineffective. Below are some of the group biases most frequently reported on boards.

Herd behavior. In general, herd behavior occurs in a group when one person believes that he or she has less information than the others. Therefore, the person is influenced by the opinion of the majority and expresses the same opinion as his or her peers without giving the matter proper consideration.

Groupthink. In overly homogenous groups, groupthink is a tendency to avoid conflict and reach consensus no matter what, which may lead to the suppression of dissenting opinions and can cause groups to lean toward conformity in perceptions and attitudes, even when those perceptions and attitudes are wrong.

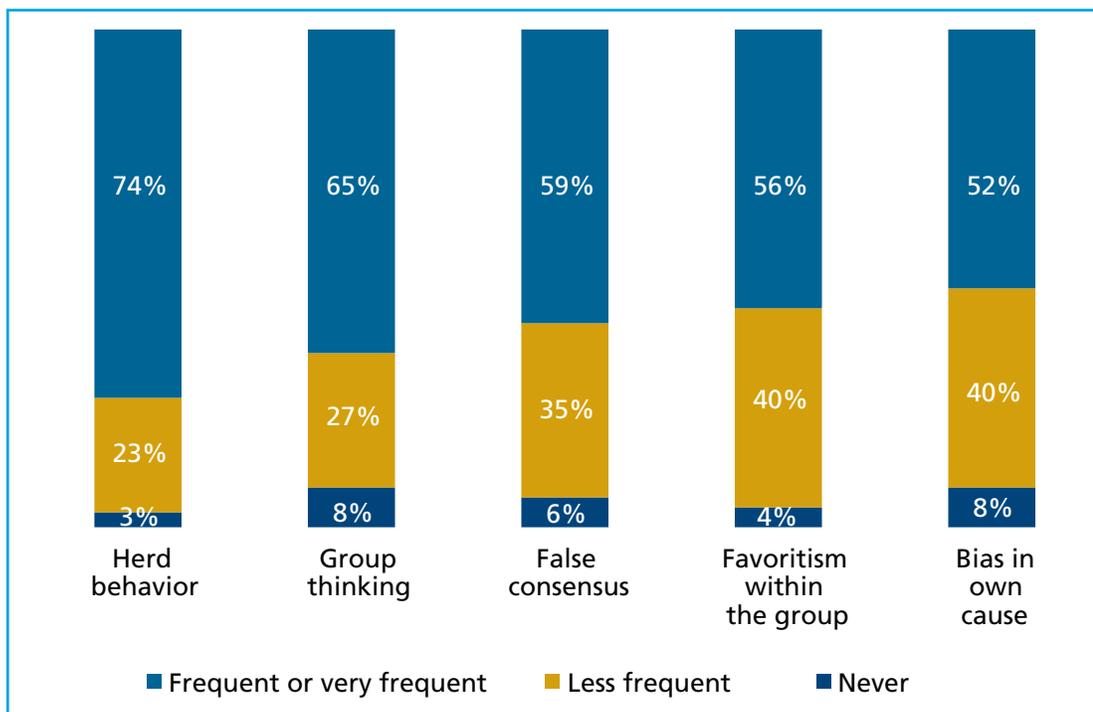
False consensus. False consensus happens when people tend to overestimate the extent to which their opinions, beliefs, preferences, values, and habits are normal and accepted by others (that is, that others also think the same way they do). This cognitive bias tends to lead to the perception of a consensus that does not exist—a “false consensus.”

In-group favoritism. This bias reveals a pattern of favoring members who belong to a certain group as opposed to those who do not. This can be seen in a board when a certain subgroup of directors (such as insiders or members of the board elected by a certain shareholder) tend to prefer proposals from their own group instead of analyzing all propositions without bias. This can also be expressed in the evaluation of others, in the allocation of resources, and in the rejection of certain issues.

Self-cause bias. This is the tendency to attribute success to internal actors and to blame any failures on external factors or third parties. This bias can limit the director’s ability to see the real facts that are causing a problem.

In our survey, we asked directors, “How frequently do you observe the following phenomena during the board’s decision-making process?” Then the survey provided a brief description of each of the cognitive biases listed above. Figure 7 presents the results.

Figure 7: Decision Making and Bias Perception



We also noted that the survey revealed an apparent contradiction: the less experienced directors were more aware of the biases. Directors with less than five years' experience on boards tended to point out cognitive biases more frequently than directors with more than 20 years' experience did. This result might lack statistical robustness, but it may indicate that younger or less experienced directors are less prone to habit or attenuation biases, both of which are situational biases, and that such directors may have a fresher and more critical view of boards.

What Directors Admit They Did Wrong

Directors—as any other decision makers in companies—make mistakes. We asked directors to look back at their own performance and consider the main factors that caused them to make bad decisions. The specific question in the survey was, “Choose up to three causes that resulted in a decision that in hindsight you consider a mistake (in a particular board situation).” It was possible to choose more than one alternative from the list provided, so the sample of 102 respondents produced 197 answers.

The factor cited most often (17 percent of total answers) was an excessive reliance on executives, which reassures us about the relevance of the oversight role that boards perform.

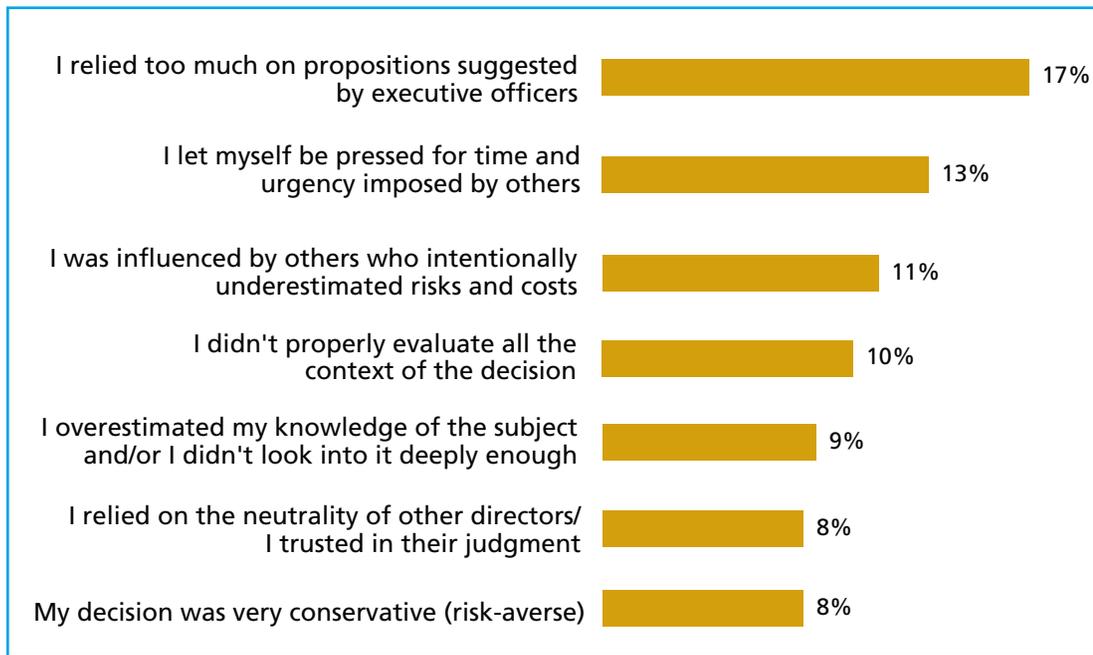
The answer that received the second-highest number of votes was “I let myself be pressed for time and urgency imposed by others.” When directors lack sufficient time to analyze their alternatives properly, they may exacerbate both individual and group cognitive biases that jeopardize decision making.

The answer that ranked third was, “I was influenced by others who underestimated risks and costs,” which alludes to groupthink and in-group favoritism, in addition to other situational biases.

The mistake-causing factor cited most often was an excessive reliance on executives, which reinforces the relevance of a board's oversight role.

The other answers directors mentioned also indicate a lack of adequate assessment of risks and costs and insufficient depth of analysis. Overall, the main sources of bad decision making are associated with 1) overconfidence, 2) being influenced by others, and 3) lack of proper analysis (risks, costs, and so on). Figure 8 shows the seven main factors that cause directors to make wrong decisions.

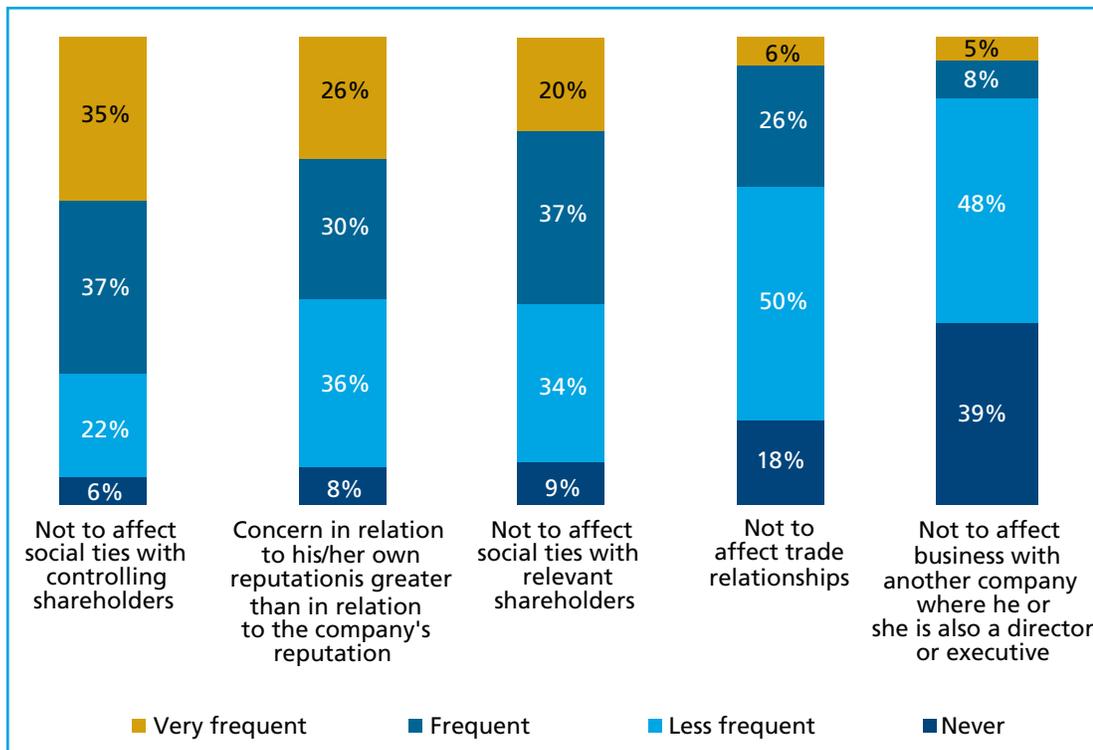
Figure 8: What Directors Admit They Do Wrong



Conflicts of Interest

Aside from honest mistakes, various conflicts of interest may lead directors to make decisions that are not in the company's best interest. We asked, "In certain situations, do you ask yourself if the other director's motivation is really the best alternative for the company or if he or she has another reason that is directing his or her behavior? What were the most frequent causes that prevented them from acting in the best interests of the company?" Figure 9 shows the percentages of the answers.

Figure 9: Reasons for Not Acting in the Company's Best Interests



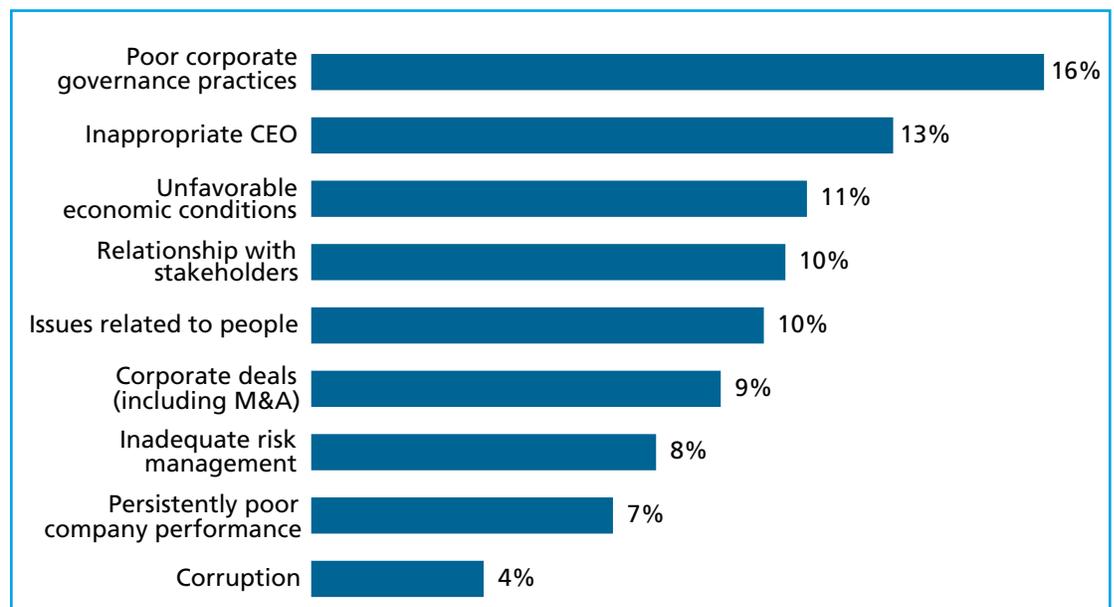
Respondents most frequently chose “not to affect social ties with controlling shareholders” to explain why directors do not act in the company’s best interests. This result is consistent with the typical Brazilian ownership structure, in which ownership is heavily concentrated among just a few controlling shareholders (as opposed to the situation found in the United States, where the dispersed ownership structure is much more common). The third answer (social ties with relevant shareholders) is also associated with the same evidence.

Other alternatives are linked to the director’s reputation and relationships with another business. About 56 percent of directors point out that frequently or very frequently their colleagues’ concern for their own reputation (rather than the company’s) has prevented them from acting in the company’s best interests.

What Keeps Directors Awake at Night?

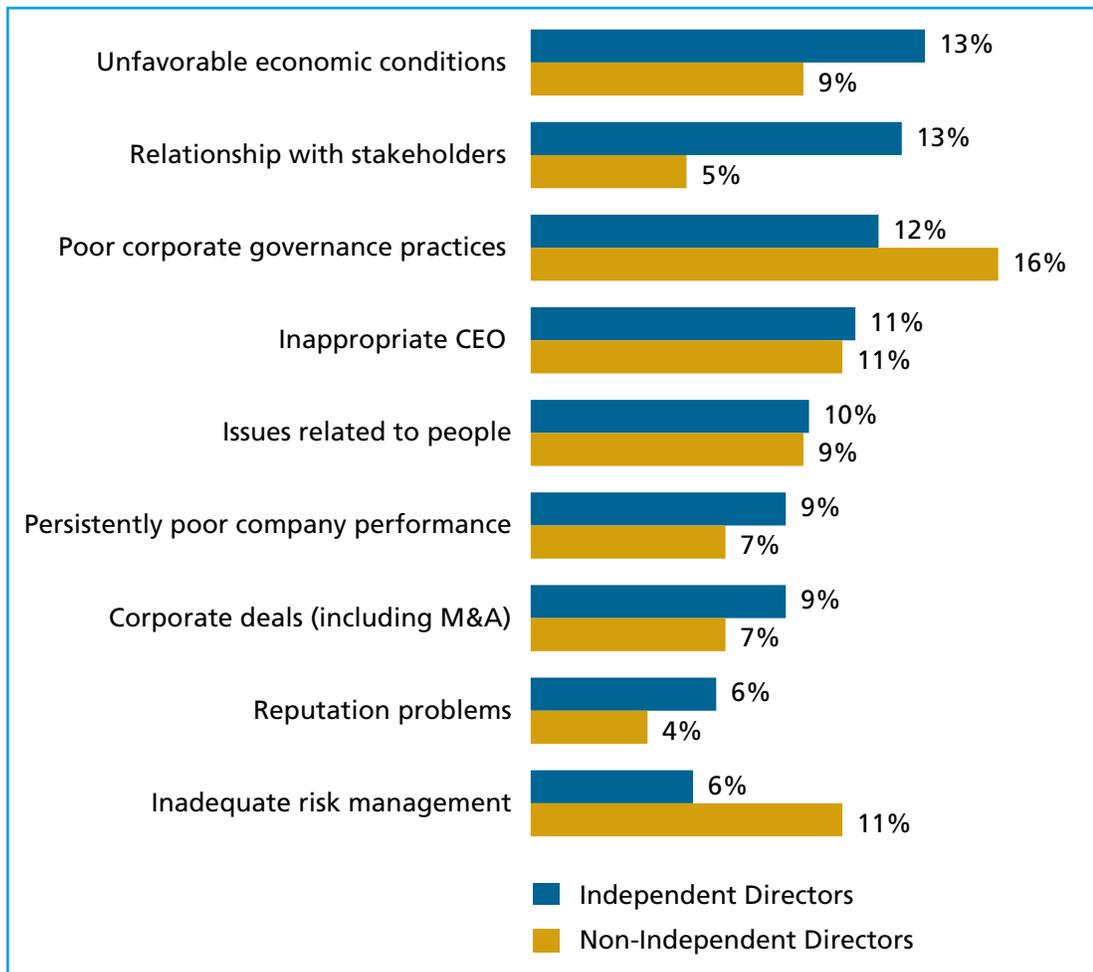
Our survey investigated the main causes of persistent concern among the directors. We asked, “Thinking generally about your experience on boards, what kind of question or situation has kept you awake at night?” The top responses were poor corporate governance practices, inappropriate chief executive officers, and unfavorable economic conditions. Corruption, a very topical subject in corporate circles nowadays in Brazil, was selected by fewer than 5 percent of directors. The top 9 (out of 13) answers account for 87 percent of the total and are shown in Figure 10.

Figure 10: Top Issues That Keep Directors Awake at Night



Here, again, independence plays an important role in the perception of directors’ concerns. In seven of the top nine answers, independent directors exhibited a higher level of concern in our survey than non-independent directors did. Regarding the relationship with stakeholders, for example, more than twice as many independent directors as non-independent directors indicated distress. Figure 11 breaks down percentages of responses by independent and non-independent directors.

Figure 11: Top Issues That Keep Directors Awake at Night —Independent versus Non-Independent Directors



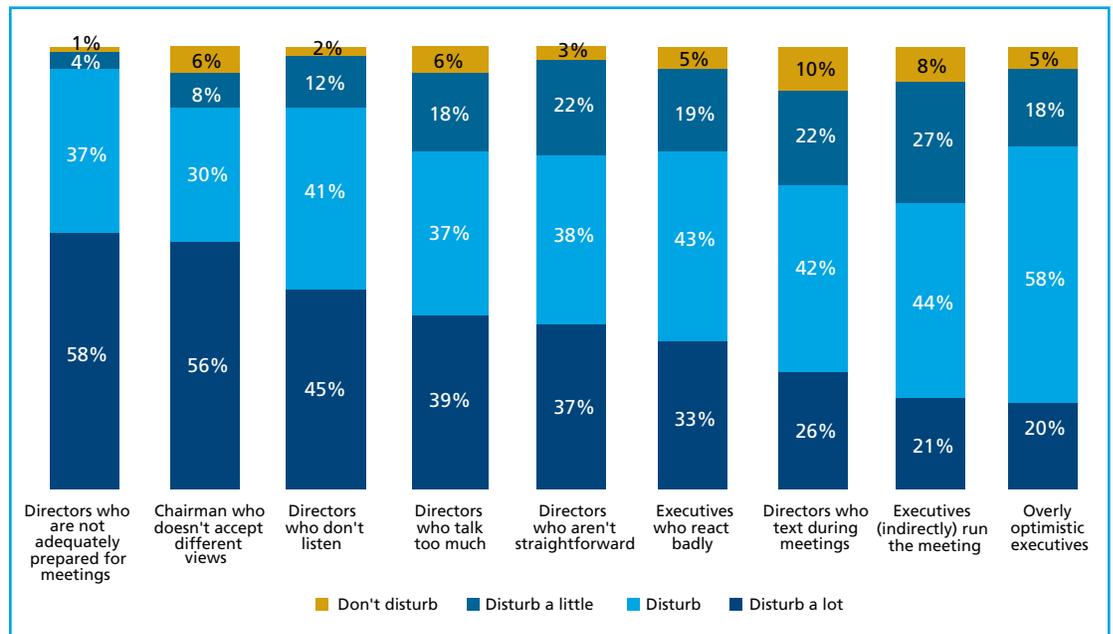
When Directors’ Behavior Threatens Proper Board Functioning

With the next questions, our survey focused on the functioning characteristics of the board, aiming to investigate how the interactions between directors influence their decisions. We asked, “What are the behavioral elements that have the greatest negative effect on the proper functioning of the board?” Responses suggest that corporate governance problems may have a negative impact, with 58 percent of the respondents saying that directors who are not adequately prepared for meetings “significantly disturb” the proper functioning of the board. Also, 56 percent say that a bossy chairman, who doesn’t accept different views, harms the proper functioning of the board.

Independent directors exhibited a higher level of concern than non-independent directors do.

“Directors who don’t listen” is listed as the third main cause restricting the board’s ability to function properly. The list also mentions other behaviors, such as “directors who text during meetings” and “directors who talk too much.” This is particularly interesting, because it highlights the importance of behavioral aspects in the success of the board. Of course, technical aspects, such as formal knowledge about a certain subject, are definitely relevant, but directors’ contributions may be significantly diminished if the behavior inside the board doesn’t create the correct atmosphere for a productive debate. Figure 12 shows the full range of results.

Figure 12: Behavior—What Prevents the Board from Functioning Well

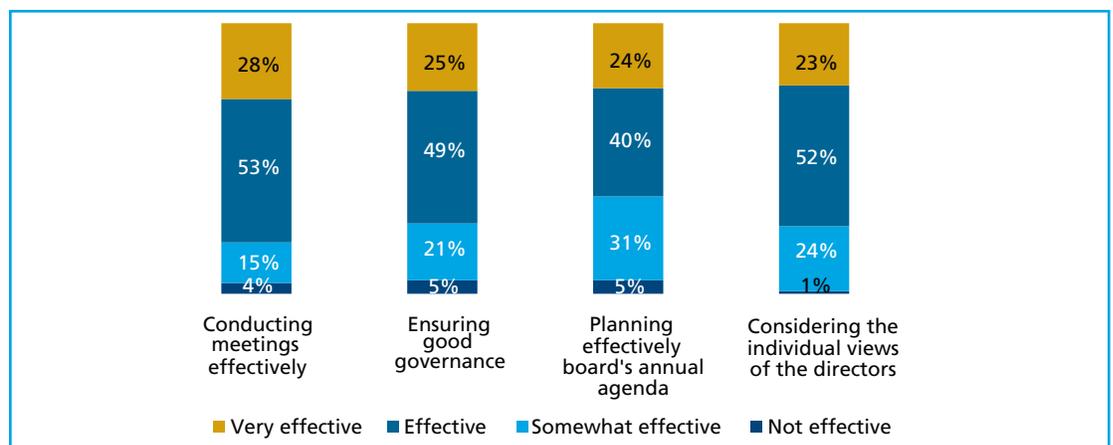


The Role of the Chairman

Strong business leaders, such as the chairmen of boards, can create an atmosphere of pressure and unease during meetings. According to KFMC (2015) research, 98 percent of chairmen had previous experience as chief executive officers. This background is usually associated with firm, autocratic professionals, often with strong personalities and a tendency to impose their views. When the chairman of the board is excessively dominant, the quality of board discussions may be diminished and may not reach the level of depth that is necessary for a correct conclusion.

We asked, “In your experience with different chairmen, how do you evaluate the effectiveness of them, regarding the following activities?” Then we listed the activities shown in Figure 13. Balancing the different views and leading the meetings in such a way as to ensure good and in-depth discussion is one of the roles of a chairman. Our survey confirms that there is room for improvement in this regard, especially when it comes to defining an effective board agenda. Of the directors participating in the survey, 36 percent suggested that the chairman was not really effective in accomplishing this task.

Figure 13: Chairman—Room for Improvement



Conclusion: Research Findings and Actual Experience

Results of this research are in line with the professional experience of the authors. For example, we were not surprised that directors chose as their main concerns merger and acquisition transactions, chief executive officer hiring and dismissal, and ownership transactions. The risk level and impact involved in such decisions are usually very high, and the decisions themselves are often enmeshed in a web of uncertainty.

Equally unsurprising is that board directors are not always right in their calls, and that—when asked whether they would have taken a different approach regarding their hardest decisions—only 24 percent of the directors admitted that they would. Why no surprise? According to what one of us, Sandra, has observed in boardrooms, for directors to admit that they would have taken a different approach after knowing the result of their decisions would be to assume they have not done their best. This level of candor is not commonly found in boardrooms—or in our research, where only about a quarter of directors owned up to having regrets.

The reasons behind directors' regrets mostly centered on overconfidence in executives' propositions, insufficient time for analysis, and lack of in-depth reasoning, which agrees with Sandra's own experience serving on different boards. However, directors admitting to being risk-averse and having overestimated their own knowledge as main causes for their regrets is a surprising fact, since overconfidence seems to prevail in boards. The board environment fosters overconfidence, as directors' individual limitations are not mitigated. For directors, the willingness to question the facts and their own certainty is just as important a tool as knowledge and experience are.

Also not surprising was the finding that independence and gender are factors that affect the behavior of directors. This research found that both characteristics influence how directors see their own decisions and how much they regret their mistakes. As in actual boardrooms, self-declared independent directors in our survey tended to find it harder to deal with subjects that encompass such big responsibilities as hiring or dismissing a chief executive officer, entering into mergers or acquisitions, or handling ownership transactions and judicial recovery. However, the questions remain: Why do they consider those decisions harder than their non-independent peers do? Is it because they act more responsibly toward all stakeholders? Or do they face more difficulties precisely because, as independent members, they lack access to information or to the right actors in the decision process? This is something that remains to be investigated.

The influence of gender is much more difficult to observe, because boardrooms are not yet sufficiently diverse—and not only in Brazil, by the way. Despite the progress in many countries—and even where the percentage of women is higher—it is still far from full parity. In Brazil particularly, women are still *rara avis* in boardrooms. In the great majority of Brazilians boards that Sandra served on, she was the only woman, and in the rare exceptions, generally it was only one other and in a single case two other women peers. In one special case she did serve on an international board where 5 out of 12 directors were women, but we should note that it was an organization where the core activity was corporate governance.

The findings that women are more prone to assume that they would have done something differently, now that they know the outcomes of their decisions, are consistent with Sandra's observations that the behavior of women may be more anchored by a sense of duty and responsibility above all than that of men. Also, the ego factor, so common in boardrooms, seems to be less pervasive with women directors. However, this conclusion has to be viewed with caution, because it is based on a subjective interpretation.

Nevertheless, this perception is bolstered by anecdotal evidence from an experienced board director in family-owned companies in Brazil. In an interview, this male director described a conflict situation between the board and the chief executive officer. According to him, the board was overreacting to an attitude of the executive—much more because of their egos than because of what the chief executive officer had actually done. The director commented, "It is important to have a good quantity of women on boards, as they are not so much influenced by the ego. A woman director may be opposed one, two, or three times, and she will simply go ahead, focused on the topic and not on her own ego. A man has more difficulty in accepting that another man is opposing him, and then his ego may enter the scene as part of the equation."

Our findings regarding conflicts of interest also align with our own observations. Sandra's experience in boards of companies with concentrated ownership in the hands of controlling owners confirms that a major reason for conflict of interest is the directors' desire to preserve social ties with controlling shareholders and other relevant shareholders. The prevailing culture does not support board members' challenging or contradicting the controlling owners. The Brazilian culture, in particular, tends to avoid conflict instead of dealing directly with it. In addition, the aura of the power of ownership—and that it is the controlling owner who elects the directors—also establishes an environment susceptible to this sort of conflict of interest.

"The elephant in the room" has been underestimated for too long.

For all the reasons discussed above, diverse thinking does not always prevail in boardrooms, as directors may have biases that prevent the diverse vision from arising. In closed groups such as a board of directors, some directors are prone to be influenced by the comments and views of others. Pick and Merchant (2010) cite excess conformity as a problem that emerges in overly homogeneous groups. The lack of diversity and contradictory opinions results in an excessive cohesion, which may lead directors to approve decisions that they will later regret—whether they admit it or not.

There is a long road ahead to increase the boards' awareness of "the elephant in the room": the behavioral aspects and the effects of cognitive bias on the working of the board. Perhaps this elephant has been underestimated for too long. Understanding biases, blind spots, and pathologies that may represent pitfalls for boards is the first step toward mitigating them and improving decision making as well as the board's supervisory role. The chairman has a pivotal role in leading the board to such understanding and can benefit importantly from taking these aspects into account when leading the board. The black box enters now into a new era that requires it to open itself to the fresh perspective of the behavioral lens—and from that, start to rethink the working and functioning of the board.

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