BOARD COMPOSITION OF TURKISH LISTED COMPANIES: IS THERE ANY DIFFERENCE BETWEEN INDUSTRIES?

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ABSTRACT

With this study, it was aimed to determine board characteristics of the companies, which are defined as CEO duality, insider/outsider ratio and size of the board, by taking into consideration the industries that the companies operate. The research related with board of directors is an important research stream. Although, many relations were investigated, few research examined whether board characteristics differ between different industries. Boards of directors are important mechanisms for Turkish organizations, since the performance of most of the organizations is directly related with these groups. Therefore, it is important to understand the characteristics of these groups. The sample of the study includes the companies which shares are publicly traded in İstanbul Stock Exchange. The results indicate that there exists no significant difference and any trend of board characteristics between the various industries, which leads to the conclusion that industry does not matter for board composition of Turkish organizations.

Keywords: *Board Size, CEO Duality, Insider/Outsider Ratio*

INTRODUCTION

Hambrick and Mason's (1984) upper-echelon theory draw attention to the research on top level executives. There are various definitions about which of the executives of the organization form the upper echelons; boards of directors are considered to be one of them (Finkelstein & Hambrick, 1990; Haleblian & Finkelstein, 1993). Most of the research on board of directors focus on some of the characteristics of board members. These characteristics that form the board composition are CEO duality, insider/outsider ratio and the size of the board which is defined as the number of the board members.

The relation between the composition of board of directors and organizational performance attracted the attention of many researchers (Zahra & Pearce, 1989; Pettigrew, 1992; Forbes & Milliken, 1999). There exists a view in the literature about board of directors, that the financial performance of the organization is related with the structure of the board of directors (Zahra & Pearce, 1989; Pettigrew, 1992; Johnson et al, 1996). Although, there is a widespread research on this relation, the findings are not consistent (Dalton et al, 1998; Dulewicz & Herbert, 2004; De Andres et al, 2005). In this study, it is argued that the inconsistency of these research findings may be due to the contextual factors in which the organizations operate.

Although, there is numerous research on the effect of board composition on organizational performance, it is important to consider the contextual factors in relation to board characteristics (Zahra & Pearce, 1989). In most of the past research on this relation, organizational context was not taken into consideration (Boyd, 1990), which forms one of the major limitations of this research stream. Zahra and Pearce (1989) point that the current conditions that exist within and outside of the organization identifies the composition of the board characteristics, and therefore organizational performance which is the result of board performance. As an example, the authors suggest that the board characteristics of a newly formed company operating in a dynamic industry would need to be different from a well-established company operating in a mature industry. So that it is important to consider the effect of industry.

Although the intersection of the organization with its environment forms an important area of research in organizational theory and strategic management literatures (Keats & Hitt, 1988) and although the main focus of strategic management is its emphasis on the organization's competitive environment (Child, 1972; Porter, 1980); the environment is not generally taken into consideration in the studies related to upper-echelons. One of the most important criticism about this research focus on this issue, that in these studies the environment in which the organization and the group have their activities are not considered (Pettigrew, 1992).

Another criticism is that, many research related to the board composition is limited to US data (Vafeas & Theodorou, 1998; Hyland & Marcellino, 2002). Therefore, research findings about the board composition of the organizations operating in other countries, and especially in developing ones will be an important contribution to the literature. Board of directors in Turkey has an important role on the decisions of organizations so the study of these groups exists as an important topic for research in Turkish context.

The organizational control mechanisms have common characteristics in developing countries, which is a central control mechanism that results from widespread family ownership, which is present even if in large scale organizations (Yurtoğlu, 2000). It is evident that the family control in organizations is common in Turkey. The widespread organizational form apart from the public enterprises is the family organizations (Gündüz & Tatoğlu, 2003). Furthermore, being highly-centralized approximately 80% of the publicly-traded organizations are controlled by families (Ararat & Uğur, 2003). The form that is frequently observed and which can maintain the family control is the holding companies (Buğra, 1994; Yurtoğlu, 2000). The family ownership and historical dependency to family resources increased the presence of family members in the management of the organizations (Gökşen & Üsdiken, 2001). In sum, the family members take place in the boards of both small and medium sized enterprises and also big scale publicly-traded organizations. The board of directors of Turkish organizations has a legal power for the control of institutional activities, therefore, boards of directors are an important disciplinary mechanism that both give advice and control the TMTs and also can supersede these groups when necessary (Yurtoğlu, 2000).

In this study, considering the above discussions, it was aimed to investigate the effect of the organizational context in terms of the industry in which the organizations operate, in a developing country. After the review of the literature, methodology of the research is discussed and major findings are listed which is followed by the discussion and conclusion of the study.

LITERATURE REVIEW

The research on the effect of the characteristics of board members to the organizational performance were undertaken within the frame of various theories (agency theory, Fama & Jensen, 1983; transactional cost theory, Williamson, 1985; institutional theory, Meyer & Rowan, 1977, DiMaggio & Powell, 1983; resource dependency theory, Pfeffer & Salancik, 1978).

Most of the research about the board of directors were related with agency theory (Zahra & Pearce, 1989). According to agency theory, boards of directors are assumed to be the groups which control the management for the sake of organizations' shareholders (Eisenhardt, 1989a; Zahra & Pearce, 1989). For this reason, the studies undertaken within the frame of agency theory focus to the processes that are inside the organization, and thus the organizational environment is not generally taken into consideration.

On the other hand, within the frame of resource dependency theory, boards of directors are considered to be boundary spanners of their organizations; and therefore they are the important actors which provide the management, necessary knowledge and resources for the activities of organizations (Zahra & Perace, 1989). One of the important principles of resource dependency theory is that the boards of directors reflect the features of the organizations' environments (Pfeffer, 1972; Boyd, 1990; Hillman et al, 2000). According to this theory, each board member brings in the organization, different connections and resources; in addition board members are selected according to their capabilities to assure important resources. Therefore, the structure of board of directors will be formed in accordance to the dependency of resource allocations of the organization (Hillman et al, 2000).

Institutional theory indicates that, organizations reflect the institutionalized and legitimized rules of their environments (Meyer & Rowan, 1977; DiMaggio & Powell, 1983). Different from the institutional and cultural perspectives, macro-institutional perspective draws attention to the multiple effects of the society in which the organizations activate. This perspective focuses on how the organizations are shaped under the effects of state, educational and financial systems, unions and work relations. Within the frame of institutional theory and macro-institutional perspective, it is argued that in general the structure of boards of directors is determined according to the institutionalized norms in the society and the organizational field. In some of the studies, it was found out that the social norms effect the selection of the CEO and the salaries of the managers (Zajac & Westphal, 1995, 1996). In most of the studies about the board of directors of Turkish organizations, in general the effect of macro-institutional environment on boards of directors are taken into consideration (Yıldırım & Üsdiken, 2005; Üsdiken & Öktem, 2008).

The literature about the characteristics of boards of directors indicate that these research were rarely undertaken within the frame of contingency theory. This might be due to the fact that environmental conditions are not considered too much within these research stream. It was assumed within the contingency theory that the organizational effectiveness, structure and other features would be formed as a result of the fit to the contingencies which in fact reflects the conditions of organizations (Donaldson, 2001). In order that the organizations to continue their activities and to be effective, the organizational structure and processes would fit to the organizational context, which is determined as environment, technology, organizational size, organizational culture and task characteristics (Drazin & Van de Ven, 1985). Therefore, for organizational performance it is important that the organizational features to be in line with the environmental contingencies. Environment forms a major contingency for the organizations; since different environments have different economic, technical and social characteristics; the strategies and structures of the organizations that have activities in different environments are also different from each other. Accordingly, the fit of organizational structure to the environment is important for organizational effectiveness (Child, 1977; Drazin & Van de Ven, 1985; Donaldson, 2001).

This forms the motivation of this research and therefore the theoretical background for this study is the contingency theory. The implication from contingency theory is that there is not one best way of corporate governance and the structures of board of directors depend on the contextual factors. In order to understand the relation of the characteristics of board of directors with organizational performance, as a first step the environment in which the organization operates should be taken into consideration.

The research findings about the relation of top management team with organizational performance are similar with the results of the research on board of directors and organizational performance. Both of these research leads to inconsistent results. In corporate governance research, most of the attention is given to the board composition and its impact on firm performance. The most common measures of board composition are the number of directors, the insider/outsider ratio of the board and CEO duality (Zahra & Pearce, 1989; Johnson et al., 1996; Dalton et al, 1998, 1999). These research are based on the premise that boards of directors in general, and the compositional characteristics of boards in particular, should influence organizational performance. However, all of these measures of board composition resulted in inconsistent findings for organizational performance.

Board Size

Jensen (1993) discusses the effectiveness of boards with more than seven to eight members. According to the author, coordination, communication and decision making will not be effective in large boards. In line with this, the results of the meta-analyses of Dalton et al (1999) demonstrate that board size is related to higher performance, and the effect was greater for smaller organizations. In addition, Yermack (1996) found out that smaller boards have a positive effect on performance. Whereas there are other studies in which the reverse relation is found to be true. Daily and Dalton (1993) and Walsh and Seward (1990) reported that performance of larger is better.

CEO Duality

When the CEO of the organization also acts as the chairman of the board, then the organization is said to have a dual-CEO. The research on the effects of CEO duality on organizational performance also yielded to inconsistent results. The findings of most of the studies indicate insignificant effects (Rechner and Dalton, 1989; Daily and Dalton, 1992, 1993; Baliga et al., 1996). In some studies, it was found out that CEO duality have a positive effect on organizational performance (Daily and Dalton, 1994), whereas some other studies indicate negative effect (Rechner and Dalton, 1991; Coles, McWilliams, and Sen, 2001).

Insider/Outsider Ratio

Johnson, Daily and Ellstrand (1996) define inside directors as the directors who are also officers of the organization, and outside directors as all non-management members of the board. According to Forbes and Miliken (1999), insider board members may view the board work as an extension of their managerial responsibilities, but it is more likely that outside board members view the tasks of the board as being distinctly different and complementary to that of management and these members are not interested in the daily operations of the organization. Although there are studies that indicate a positive relation between the percentage of outside directors and firm performance (Schellenger et al, 1989; Pearce & Zahra, 1992; Daily & Dalton, 1993), many more others indicate insignificant results (Hermalin & Weisbach, 1991; Daily & Johnson, 1997; Dulewicz & Herbert, 2004). The results of the meta-analyses on board composition and organizational performance by Dalton, Daily, Ellstrand and Johnson (1998) indicate insignificant relation of insider/outsider ratio and organizational performance. In addition, the results of another meta-analyses conducted by Wagner et al, (1998) indicate that board size may be more important for organizational performance instead of the number of insider and outsider directors.

Within this frame, in this study, it was aimed to understand whether or not there exists a difference between the boards of directors of organizations in terms of the board composition, according to the industry in which the organizations operate, and it was suggested that there exists a difference of board compositions of organizations between industries:

H_1: The board compositions of the organizations differ according to the industries in which they operate.

METHODOLOGY

The purpose of this study was to investigate the board compositions of the companies whose shares are publicly traded in İstanbul Stock Exchange (İSE), in accordance to the industry in which they have their organizational activities. The research questions were:

- What is the average board size of the companies listed in İSE?
- Is CEO duality common between these companies?
- What is the average insider/outsider ratio for these companies?
- Do the board compositions of these companies differ according to the industries in which they operate?

It was suggested that the board compositions of the companies listed in İSE will differ from each other due to the specific characteristics of the industries which the companies should fit their board composition accordingly.

Websites of the companies are useful tools to communicate the company's values and policies. Publicly traded companies should have information related with their board of directors, announced via their web-pages according to the Corporate Governance Rules published by Capital Markets Board of Turkey. Data was collected through the websites of the companies whose shares are publicly-traded in the national market of İSE. The sample does not include the companies which their shares are traded in secondary national market, watch-list companies market, new economy market, fund market; and the ones whose shares are temporarily forbidden from the transactions. Apart from 54 such companies; there are 287 companies whose shares are publicly traded in the national market, and the sample of this study contained all of these companies. Annual activity reports were investigated for the size of the board and CEO duality, and in addition corporate governance reports were investigated for insider/outsider ratio of the boards. After the collection of the data, the variables were coded and analyzed by SPSS 15.0. The descriptive statistics of the board compositions of the organizations are summarized below in Table-1:

Table 1. Board Characteristics of the Sample

CEO Duality	Frequency	Percent
No Duality	128	44,6
CEO is also Board	139	48,4
CEO is also	20	7,0
Outsider Ratio	0,0	1,00

	Minimum	Maximum	Mean
Board Size	3	15	6,56
Number of Insiders	0	7	1,23
Number of Outsiders	0	13	5,33
Insider Ratio	0,0	1,00	0,1922
Outsider Ratio	0,0	1,00	0,8078

Table 2. Industries included in the Sample

Industry	Frequency	Percent
Mutual Funds	35	12,2
Textile & Clothing	23	8,0
Food & Beverage	21	7,3
Holding & Investment	17	5,9
Banking & Finance	17	5,9
Cement	17	5,9
Real Estate Investment	13	4,5
Iron, Steel & Metal	13	4,5
Technology & Communication	12	4,2
Chemicals	11	3,8
Electrical Equipments	11	3,8
Automotive	10	3,5
Paper	8	2,8
Petroleum & Coal	8	2,8
Glass, Glassware, Earthenware & Porcelain	7	2,4
Insurance	7	2,4
Leasing & Factoring	7	2,4
Publication	6	2,1
Metal Products	5	1,7
Other manufacturing	5	1,7
Retail Trade	5	1,7
Services	5	1,7
Tourism	5	1,7
Construction	4	1,4
Electricity, Gas & Steam	4	1,4
Sports	4	1,4
Transportation Services	4	1,4
Woodwork, Timber & Furniture	3	1,0
Total	**287**	**100,0**

In most of the studies, organizational environment is considered as the industry that the organization operates. In this study, also industry was considered to be the organizational environment. The information about industry codes for these companies was available from Capital Markets Board and İSE. Initially, the number of the industries in which the companies operate were found out to be 48. In order to have a comparative basis between the industries, the industries were grouped under the wider industry codes and the total number of industries for the study was 28. The descriptive statistics for these industries are listed in Table-2.

FINDINGS

As demonstrated in Table-1, the board size of the organizations range from minimum 3 members up to 15 members at most. The boards are composed of approximately 7 members on the average. It can be observed that, most of the organizations operating in banking and finance industry have more than 8 board members; and besides, about 43% of the organizations operating in mutual funds industry have less than 5 board members (Table-3).

When insider and outsider directors are considered, it is noticed that the average of insider directors are much more less than outsider directors (Table-1). In Table-4, CEO duality is demonstrated taken the industries in which the organizations operate, into consideration. In about 45% of the organizations, the positions of CEO and chairman are separated from each other (Table-1). The separation of these roles is one of the major requirements of Capital Markets Board, and it is observed that most of the companies (93%) obey to this rule. However, although CEO duality is very low (7%), a board member to function as a CEO is a common application (48,4%) among the organizations. This emerges as another way of board control over the management of the organization.

On the other hand, the ANOVA analysis indicated that, there has been no statistically significant difference of the board size, CEO duality and insider/outsider ratio between the industries, which does not support the proposed hypothesis.

Table 3. The number of Board Members by Industry

	Board Size			
Industry	**Less than 5 members**	**5-8 members**	**More than 8**	**Total**
Automotive	0	8	2	10
Banking & Finance	0	5	12	17
Cement	0	11	6	17
Chemicals	1	9	1	11
Construction	0	3	1	4
Electrical Equipments	0	10	1	11
Electricity, Gas & Steam	0	4	0	4
Food & Beverage	4	14	3	21
Glass, Glassware, Earthenware & Porcelain	0	6	1	7
Holding & Investment	0	8	9	17
Insurance	0	5	2	7
Iron, Steel & Metal	3	8	2	13
Leasing & Factoring	0	7	0	7
Metal Products	1	4	0	5
Mutual Funds	15	20	0	35
Other manufacturing	0	3	2	5
Paper	0	5	3	8
Petroleum & Coal	0	6	2	8
Publication	0	5	1	6
Real Estate Investment	2	9	2	13
Retail Trade	0	2	3	5
Services	1	4	0	5
Sports	0	3	1	4
Technology & Communication	3	8	1	12
Textile & Clothing	5	16	2	23
Tourism	0	5	0	5
Transportation Services	0	3	1	4
Woodwork, Timber & Furniture	0	3	0	3
Total	**35**	**194**	**58**	**287**

Table 4. CEO Duality by Industry

	Board Size			
Industry	**No Duality**	**CEO is also Chairman**	**CEO is also Board Mem-**	**Total**
Automotive	5	0	5	10
Banking & Finance	0	2	15	17
Cement	13	2	2	17
Chemicals	4	1	6	11
Construction	1	0	3	4
Electrical Equipments	5	1	5	11
Electricity, Gas & Steam	1	0	3	4
Food & Beverage	13	2	6	21
Glass, Glassware, Earthenware & Porce-	5	0	2	7
Holding & Investment	3	2	12	17
Insurance	0	0	7	7
Iron, Steel & Metal	8	0	5	13
Leasing & Factoring	1	0	6	7
Metal Products	2	0	3	5
Mutual Funds	17	3	15	35
Other manufacturing	1	1	3	5
Paper	5	0	3	8
Petroleum & Coal	6	0	2	8
Publication	4	0	2	6
Real Estate Investment	6	2	5	13
Retail Trade	3	0	2	5
Services	3	1	1	5
Sports	4	0	0	4
Technology & Communication	4	1	7	12
Textile & Clothing	8	1	14	23
Tourism	3	0	2	5
Transportation Services	2	0	2	4
Woodwork, Timber & Furniture	1	1	1	3
Total	128	20	139	287

DISCUSSION AND CONCLUSION

The board compositions of publicly traded Turkish organizations were examined with this study. The results of this research indicate that board composition of these organizations in terms of their number of board members, CEO duality and insider/outsider ratios of the directors; do not significantly differ between the industries in which the organizations operate. Although, Yurtoğlu (2000) in his research found out that board size differ significantly between different industries, the findings of this study are not similar. According to the results of Yurtoğlu's (2000) research, holding companies and financial companies have larger boards than manufacturing companies. The conflicting findings of this study, with the study of Yurtoğlu are probably due to effect of time. Yurtoğlu's research was conducted with 1998 data, and the data for this study was from 2008. The results of this current study indicate that within 10 years time, board size of the companies operating in different industries converged to each other.

With this study, it was found out that the average number of board members is approximately 7, outsider directors are more common for the management and although most of the chairmen do not hold the position of CEO at the same time, instead one of the board members holding the CEO position is a common application among the organizations. This board member is usually the vice chairman. This is an implicit indication of board control over the management. From one side, the organizations obey the requirements of Capital Markets Board but on the other side they still maintain the control.

The findings of this study suggest that industry does not make a significant difference between the boards of the organizations. This may be related to the representation of most of the family members as board of directors. Since family members dominate the boards of the organizations, industry specific features might not matter for the organizations. Similarly, Yurtoğlu (2000), in his study examining 257 publicly traded Turkish companies, also found out that the majority of the companies investigated were ultimately dominated and controlled by families. This result is also supported with another study of Yurtoğlu (2003) in which 305 publicly listed companies was investigated.

Although this study enhances the understanding of the board composition of publicly traded organizations, further research on the topic should also address the relation of board composition with the organizational performance between different industries. This relation was not taken into consideration which forms the major limitation of the study.

Despite this limitation, it is to our knowledge that there are no empirical studies that address industry differences of board composition of organizations in terms of the three dimensions of board composition, in Turkey. Further research in this area might increase awareness and understanding of the effect of different contextual factors other than the industry on the board composition of the organizations.

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