

# The Impact of Shareholder Involvement in the Nomination Process on Board Diversity

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## Abstract

*Controlling the composition of the board is important in corporate governance. In order to prevent incumbent members to capture the nomination process, an external nomination committee has been introduced in some Nordic countries. In Finland both internal and external nomination committees are used by listed companies. This feature provides an ideal case to test whether differences in nominating board members make a difference for board composition. Companies with a nomination committee composed of a group of external experts have, on average, more female directors on their boards, but less international diversity and less diversity in terms of age dispersion and director tenure. However, these differences become non-significant when the voting rights of the largest shareholders are included in the regression analysis. The results suggest that when ownership structure is taken into account the procedure used to select director candidates has a limited impact on the final board composition or diversity.*

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## 1. Introduction

As board composition is important for company success, the procedure used in the selection of board members is a crucial element of corporate governance. The selection procedure for director candidates in some Nordic countries is unique in the European context, and was designed to emphasise the relevance of active ownership through control of owners. In some Nordic countries companies may choose to have a nomination committee composed of external experts, who are elected directly by the (usually three) largest shareholders. Although in theory more than one board member may be appointed to this kind of nomination committee, in practice the number of directors is usually limited to one member. This control by large shareholders of the selection process gives the three largest shareholders (those that select the members of a nomination committee) a disproportionate power with respect to other owners, incumbent board members and charismatic CEOs. Such a nomination procedure is prevalent in Sweden and Norway, and is widely used in Finland.

By contrast, in the UK and Continental Europe candidates for board positions are usually nominated by a committee composed of a majority of independent board members. These members select a pool of candidates which the board presents at the AGM for majority voting. This method of nominating candidates has been questioned, as directors who control the nomination process might not just be concerned about shareholders' interest, but also about their own career and their position within the board. As a result, they may choose potential candidates based on their own interests or career concerns, rather than on the match between the company's needs and the candidates' merits or abilities. Incumbent directors may prefer as peers people with whom they share common ground, to save time in decision making processes and to benefit from group loyalty (Zander, 1979), mentoring (Athey, Avery and Zemsky, 2000) and trust (Kanter, 1977), which depend on group members' similarity. Besides, they are subject to bounded rationality and may prefer

to work with those who are like them and whose characteristics they believe they know well (Rui-grok, Peck and Tacheva, 2006). They might also prefer less demographical diversity to avoid costs of language change (Piekkari, Oxelheim and Rando-y, 2013). These aspects lead to the assumption that incumbent board members tend to prefer less diverse boards. If this preference prevails in the selection of director candidates, less board diversity can be expected when the nomination process is controlled by board members.

External nomination committees have been designed to prevent personal preferences of committee members to prevail over shareholder interests in the selection of director candidates. Because the members of the external nomination committee are not board members, they are not bound to group loyalty, trust or bounded rationality. This lack of personal preference for similarity would result in companies with external nomination committees having more diverse boards than those where an internal nomination committee is in place.

The validity of this statement is tested through an analysis of the extent to which different types of nomination committee lead to actual differences in board diversity. In the empirical analysis the relationship between the type of nomination committee used and measures of board diversity, such as the number of female directors, internationalisation of boards, age dispersion of board members, and dispersion of board members' time served on the board is documented. It is seen that companies with an external nomination committee (elected by the largest shareholders) have, on average, more female directors on their boards, but have less demographic diversity and less diversity in terms of age dispersion and time served on the board of their directors. Controlling for ownership, governance, and company characteristics, these differences become statistically insignificant. Thus, the findings do not support the view that incumbent directors who are members of a nomination committee use their position to promote socially homogeneous boards.

Additionally, the extent to which differences in

the type of nomination procedure are significantly related to differences in board size, independence, and average age and time served on the board of directors is explored. It is important to control for the fact that larger or more independent boards have more avenues for diversity than smaller and more concentrated ones. To test differences in board composition in relation to the type of nomination committee, regression analyses are included, where board size, average age of board members, board independence, and average time served on the board of directors are regressed on the type of nomination procedure along with company-level controls. No significant differences in terms of board size, independence, or average age of board members is found.

There is therefore no evidence that suggests that directors who are members of nomination committees use their influence to select director candidates who are similar to them in order to achieve a more homogeneous board. There are no significant differences between both groups of companies in terms of board diversity, board size, independence, or directors' age, suggesting that members of nomination committees, whether comprised of incumbent directors or external experts, have the same preferences for director candidates. Boards whose candidates are selected by an external group of experts are less stable and change their members more often, but are still more homogeneous in terms of board members' age and seniority.

The analysis exploits differences in the recommendations for the establishment of nomination committees in the Finnish Corporate Governance Code. The case of Finland is unique, as Finnish Corporate Law and the Corporate Governance Code give companies freedom in the design of their corporate governance structure. Both external nomination committees elected by the largest shareholders and internal nomination committees composed of board members are included in the Finnish Corporate Governance Code as recommended nomination procedures (Finnish Corporate Governance Code, 2010). In other countries, such as Sweden, the Code Recommendations

only provide for an external nomination committee. This difference in Codes is not trivial: while in Sweden the use of an external group of experts is prevalent (only 3% of the Swedish listed companies do not comply with the Code Recommendations for nomination committees), in Finland there is more variety in the manner in which board members are elected (38% of listed companies in Finland have an external nomination committee, 24% have a board-internal nomination committee, and the rest have no formal procedure in place for the selection of candidates for board positions). This variety in nomination procedures in Finland affords a unique setting for testing whether the method used to nominate director candidates has an impact on final board composition.

In recent years board diversity has been promoted at European, Nordic, and national levels, and has triggered a raft of literature analysing the antecedents of diversity, and its impact on performance, (Ferreira, 2014; Adams, De Haan, Terjesen and Van Ees; 2014; Adams and Ferreira, 2009; Piekkari, Oxelheim and Randoy, 2013; Bohren and Staubo, 2014; Ahren and Dittmar, 2012; Kaczmarec, Kimino and Pye, 2012 among others). This study contributes to this literature by examining whether it might be possible to promote diversity through the choice of selection process. It expands the concept of diversity to include aspects such as age diversity and time served on the board of directors that influence board work-functioning and performance.

The study also adds to the literature that analyses the role and impact of committees in and on board design (Walther and Morner, 2014; Rui-grok, Peck, Tacheva, Greve and Hu, 2006). This literature deals with the internal functioning of the board in committees to facilitate delegation of authority and information transmission, and to mitigate coordination and free-riding problems. Corporate Governance Codes in Nordic countries provide detailed recommendations for the establishment of nomination committees. These detailed recommendations contrast with the lack of empirical research on the adequacy of nomination committees to improve company governance in

the Nordic context, and on how the type of nomination committee might affect the final structure of the board in a system devised to ensure that a dominant shareholder can govern the company.

Finally, this study also contributes to the literature that analyses the conflicts of interest between large and small shareholders. It contributes to the analysis of the selection procedure from the perspective of social embeddedness (Winters, Hillman and Cannella, 2012). In a company with an external nomination committee the three largest shareholders directly select board members. This control of the selection process by large shareholders gives the three largest (those that select members of the nomination committee) a disproportionate power with respect to the other owners. In this case, the study examines whether board composition and diversity is affected by this power.

The rest of the paper is organised as follows: the Finnish Corporate Governance system is described in Section 2; in Section 3 the data is presented; empirical results are presented in Section 4; robustness tests are presented in Section 5. Section 6 concludes.

## 2. The Institutional Framework

Corporate Governance in Finnish companies follows the key features of the Nordic Corporate Governance model, such as one-tier boards with a limited number of managers, concentrated ownership with active owners, and clear separation of the positions of CEO and chairman (See Liljebloom and Loflund, 2006; Maury and Pajuste, 2002 and Maury and Pajuste, 2005).

The importance of the informal norms is illustrated by the fact that, although the Code and the Finnish Companies Act give a lot of freedom to companies to design their corporate governance structures, these governance structures share many common features. For example, although both chair duality and two-tier board structures are allowed in Finland, they are very rare in practice. Managers are usually absent from Finnish

boards, although neither the Code nor the Companies Act place a limit on the number of managers who may belong to the board.

The typical Finnish board has a one-tier board structure, and the participation of management team representatives is usually limited to one member. There is no formal division between management and supervision. In general, unlike in English-speaking countries, the Nordic codes do not advise that the majority of board members be independent of shareholders<sup>1</sup>. The Finnish Code recommends that “at least two directors should be independent of owners and major shareholders”.

The largest owners are usually represented on the board, as ownership concentration is considered a strong corporate governance mechanism in Finland. These strong owners are encouraged (by the Code and common norms) to actively engage in the governance of their investee corporation. It is also the case that in the Nordic countries (and in Finland in particular) smaller shareholders are widely protected by law. The company acts of the Nordic countries allow for substantial protection of minority owners. There are a number of rules limiting the majority decision principle on specific matters at the General Meeting, requiring a certain number of decisions for various degrees of qualified majority of both shares and votes to be valid (Gregoric, Oxelheim, Randoy and Thomsen, 2009).

The Code and Regulations give a lot of freedom to Finnish companies to design their governance structure. This freedom results in a more diverse pool of governance uses than in other Nordic countries. The Code gives freedom where the nomination of board candidates is concerned. Finnish companies can choose to have a nomination committee composed of board members, or they can opt for a nomination board (referred to as an “external nomination committee” throughout this text), composed mainly of non-board members, and elected by the largest shareholders. Both types of nomination procedure comply

<sup>1</sup> Henceforth, an independent board member is denoted as one who is independent both of the management and of the largest shareholders of the company.

with Recommendation 22 of the Finnish Corporate Governance Code (2010)<sup>2</sup>. A “representative” external nomination committee is composed of three to four members, usually the chairman of the board of directors and two to three external members. This external nomination committee is not considered a departure from the Code, as long as the election process, its composition and operations are properly disclosed.

In short, the two types of nomination procedure proposed by the Finnish Code differ in three main respects. The first difference lies in their composition: members of an internal nomination committee are incumbent directors, while members of external nomination committees are external experts, who are neither board members nor members of the management team. The second relates to who is responsible for selecting those members. Internal nomination committees are subrogating board structures, whose members are elected by the board’s other members. On the other hand, the largest shareholders directly elect experts who are members of the external nomination committee. Finally, both types of selection procedure differ in their accountability: the internal nomination committee, being a subrogating board structure, presents its candidates to the board, which in turn presents them to the AGM for election. In the case of an external nomination committee, the board of directors is not involved at any stage of the selection process. The three largest shareholders elect the members of the external nomination committee, which in turn presents its candidates directly to the AGM.

To find suitable directors the nomination committee (of any type) must have access to up-to-date and relevant information on the company’s position and strategy. The chairman of the board is the main source of information concerning the board, its members, and the work undertaken. Most of this information is therefore collected from the chairman. Moreover, the nomination committee must have access to the mandatory annual written evaluation of the board required by the code. The

chairman of the board is usually a member of the nomination committee, and is responsible for the communication of essential information during the selection process.

### 3. Description of Data and Univariate Tests

#### 3.1 Description of Data

There were approximately 105 non-financial companies listed on OMX Helsinki in December 2013 (Lekval, 2014). Of these, forty had established an internal nomination committee composed of board members, and less than one third (25 companies) had an external nomination committee elected by their largest shareholders. The remaining companies had no established formal nomination procedure. From Table 1, it can be seen that most companies that had not set up a nomination procedure of any kind were small, while most companies in the large and medium capitalisation segments either had a nomination committee composed of board members or an external nomination committee appointed directly by their largest shareholders.

In all, the dataset comprises 328 observations. These observations relate to all Finnish non-financial companies listed on the OMX Helsinki index that had a nomination committee (of any kind) between 2008 and 2013. Some companies delisted before 2013, but which were active in 2008 (for example Okmetic Oy, Inion Oy, Talvivaara Oy, Powerflute Plc) have been included. The sample contains only those company-year data points where a nomination committee is reported in the annual reports. This means that the panel is unbalanced.

Information on these companies has been obtained from various sources. Information on nomination committees has been hand-collected. Director characteristics have been partly obtained from BoardEx and partly hand-collected. Information on company characteristics has been obtained from FactSet. Information on ownership has been hand-collected in the case of dual class

<sup>2</sup> Both types of nomination procedures comply also with the new Finnish Corporate Governance Code (2015).

Table 1. Type of nomination committee and market segment.

SEGMENT	TYPE OF NC			TOTAL
	INTERNAL TYPE OF NC (NC-DUMMY=0)	EXTERNAL TYPE OF NC (NC-DUMMY=1)	NC NOT ANNOUNCED	
Large Cap	14	8	4	26
Medium Cap	16	11	8	33
Small Cap	9	5	32	46
Total	40	25	40	105

Note: This table reports how non-financial companies listed on NASDAQ OMX Helsinki (December 30 2013) are distributed by market segment and type of nomination committee. Each row represents the total number of companies in each market segment. Each column shows the type of nomination committee. The last row shows that there were 105 non-financial companies listed on NASDAQ OMX Helsinki by the end of 2013. Of these, 40 companies have a nomination committee composed of board members, 25 companies have an external nomination committee, appointed by the largest shareholders and composed of a majority of non-directors, and 40 non-financial companies have not established a formal nomination procedure in their annual reports.

share companies (19% of observations), and has been obtained from Thomson One in the case of companies with only one share type.

The key variable in the analysis is a dummy variable (*NC-external dummy*), which takes the value one if the company has a nomination committee that is elected directly by the largest shareholders and is composed of a majority of non-board members. It takes the value zero if the company has a nomination committee elected by the board and composed of a majority of board directors.

Diversity is measured along various dimensions. Gender diversity is measured by the number of females on the board (*female*), the ratio of females to board members (*% females*) and a dummy that takes the value one if at least one female director sits on the board (*female dummy*). International diversity is measured by the total number of foreign directors (*foreign*), the proportion of foreigners on the board (*% foreigners*) and a dummy that takes the value one if at least one board member is not Finnish (*foreign dummy*).

Additional measures of dispersion are the age dispersion of board members (*sd age*) and the dispersion of time served on the board (*sd time on board*), measured as the standard deviation of age and time served in the role of members of the board of directors.

Board composition is measured using the total number of directors (*board size*), their average age (*av. director age*), their average time as board members (*av. time on board*), and the ratio of inde-

pendent directors to board size (*% independent*).

Two measures of board turnover are included. The variable *number of new directors* measures the number of directors who have served less than a year. *Board renewal* is defined as the proportion of new directors to board size.

Ownership is characterised as the percentage of voting rights. Three variables are included that measure the voting rights of the three largest owners separately (*% voting largest, second largest, and third largest*), and one variable (*sum voting*) which is the sum of the voting rights of the five largest owners. Only the three largest owners in the individual variables are included, because regression results underline the significance of the largest owner. The five largest owners in the aggregate measure (*sum voting*) are included to make the robustness tests more informative.

Company characteristics are *total assets* in millions (assets), *leverage* (measured as total debt to total assets), *ROA*, and *net income*. In the regressions total assets are included in logarithmic form, and ROA and net income are lagged one period.

Descriptive statistics for the main variables in the analysis are presented in Table 2.

The data is in line with previous studies on Finnish data. For example, it reports an average board size of 6.91, while in Gregoric , Oxelheim, Randoy and Thomseen (2009) the average Finnish company has 5.97 board members. The average director is 55.31 years old and has served on the board for 4.96 years, whereas Gregoric *et al.* find

Table 2. Descriptive statistics

VARIABLE	OBS.	MEAN	ST. DEV	MAX	MIN
<b>NOMINATION COMMITTEE</b>					
NC-external dummy	328	0.427	0.495	0	1
Board diversity					
Number of females	328	1.47	0.976	0	5
% females	324	0.207	0.13	0	0.83
Female dummy	328	0.86	0.348	0	1
Number of foreigners	328	2.43	2.15	0	9
% foreigners	324	0.3389	0.289	0	1
Foreign dummy	324	0.728	0.445	0	1
Age dispersion	290	7.29	2.4	1.9	16.4
Dispersion of time served on board	328	3.02	1.86	0	10.6
<b>BOARD COMPOSITION</b>					
Board size	328	6.91	1.41	3	11
Av. director age	328	55.31	3.42	41.3	63.57
Av. time on board	328	4.96	2.11	0.33	15
% independent	324	0.82	0.187	0	1
Board turnover					
Number of new directors	328	1.07	1.08	0	5
Board renewal	324	0.15	0.15	0	1
Ownership					
Dual class shares	328	0.19	0.39	0	1
% voting largest owner	308	0.169	0.142	0.0008	0.67
% voting second largest owner	308	0.069	0.047	0	0.278
% voting third largest owner	308	0.0457	0.027	0	0.12
Voting rights of the five largest owners (sum)	308	0.32	0.171	0.0017	0.86
<b>COMPANY CHARACTERISTICS</b>					
Assets	328	2884.98	6004.6	11.2	39582
Leverage	324	0.269	0.143	0	0.894
Lag ROA	327	3.09	8.92	-50.86	28.81
Lag net income	328	104.91	31	-3104	3988

Note: This table presents descriptive statistics of all variables included in the analysis. A definition of each individual variable is presented in the data section.

that the average director of a Finnish company is 53.72 years old and has served for 5.14 years.

When the diversity of Finnish companies in Gregoric *et al.*'s report is compared with the data for the period 2008–2013, it can be seen that boards have become more diverse in terms of both gender and demography. The percentage of female directors in the data (average, 2008–2013)

is 20%. This figure is significantly larger than the 11.60 % reported by Gregoric *et al.* for 2007. The percentage of foreigners on the board in the data is 33.89%, whereas Gregoric *et al.* reported an average of 13.7% for 2007. The percentage of companies with at least one foreign board member has increased from 19.48% in Gregoric *et al.* to 23.2 % in the data.

Two trends are observable from Figure 1, which is based on annual data. The first is an increase in the number of companies that chose to establish a formal procedure for the selection of director candidates. The second is a preference for board-internal nomination committees.

Figure 1 shows that the number of companies in the dataset increases from 40 in 2008 to 65 in 2013. The number of companies with an internal nomination committee increases from 22 in 2008 to 40 in 2013. The number of companies that have an external nomination committee has increased from 18 to 25 in the same period. In practice, it is very rare that companies change the type of nomination committee used (from internal to external or *vice versa*). It can also be seen that companies rarely abandon nomination committees once they have started to use them. The increase in the number of companies with a formal nomination procedure explains the increase in the number of observations per year in the dataset, although the number of listed companies in Finland has remained fairly constant throughout the years of the study.

A preference for nomination committees composed of board members is very clear, especially after 2010, when the new Corporate Governance Code was published. With the publication of the 2010 Code, most listed companies, especially larger ones, started to publish their own Corporate Governance Statements, and established written procedures for corporate governance practice. The increase in the number of companies with a formal nomination procedure may reflect companies' efforts to increase their corporate governance standards.

For the first time the 2010 Code introduces the possibility of having an external nomination committee formed by a group of experts, whereas the first Finnish Corporate Governance Code of 2008 allowed for internal nomination committees (composed of board members). One might expect the introduction of a new nomination procedure in the code to be reflected in a shift towards its adoption, but this was not the case in Finland. An increase of 38% was observed in the number of companies with an external nomination committee, although the number of companies that chose to have an internal nomination committee almost

doubled in this period. The trend over time shows a preference for internal nomination committees, although the number of companies with an external committee has also increased.

It is worth noting that the change in the type of nomination committee in Finland is infrequent. Our data show that once Finnish companies choose to set up a nomination committee they rarely change its type. Only in three out of 328 observations there is a change from an internal to external nomination committee, and we have not observed any change from external to internal committee. We have never observed a change from having a nomination committee (of any type) to having no nomination committee at all. Once a type of nomination committee is set up, its use usually continues irrespective of changes in ownership concentration, board composition or firm performance.

Figure 2 shows that gender and demographic diversity have increased during the sample years, although board size has remained fairly constant.

Gender diversity has been promoted by regulators in Nordic countries. Although no quotas have been imposed, the ninth recommendation of the CG Code of 2010 states that "both genders shall be represented on the board". In the sample more than 86% of the company-year observations comply with this recommendation (97% of the companies in the data complied with this recommendation in 2013). On the average board 25% of directors were women in 2013, whereas only 15% were in 2008.

International diversity has also increased in the years of the study. The number of foreigners on Finnish boards has increased from an average of 1.9 in 2008 to 2.73 in 2013. In 2008 65% of Finnish non-financial listed companies had at least one foreigner on the board<sup>3</sup>, whereas in 2013 this figure was 77%.

In line with previous studies it can be seen that features of board composition such as board size and average board age have not changed significantly in the period 2008–2013. The diversity of

<sup>3</sup> Gregoric A., Oxelheim, Randoy and Thomsen, (2011) report that by 2008, 50% of Nordic companies had at least one international director.



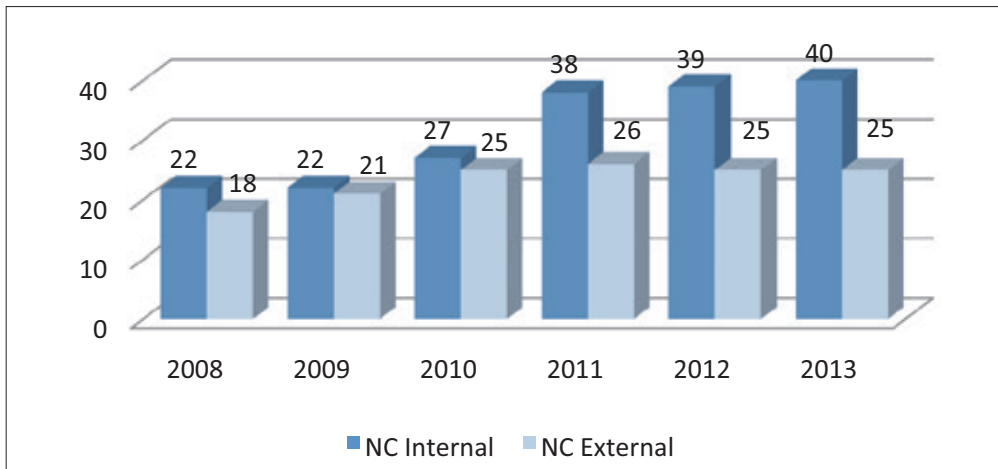


Figure 1. Number of Companies by kind of NC

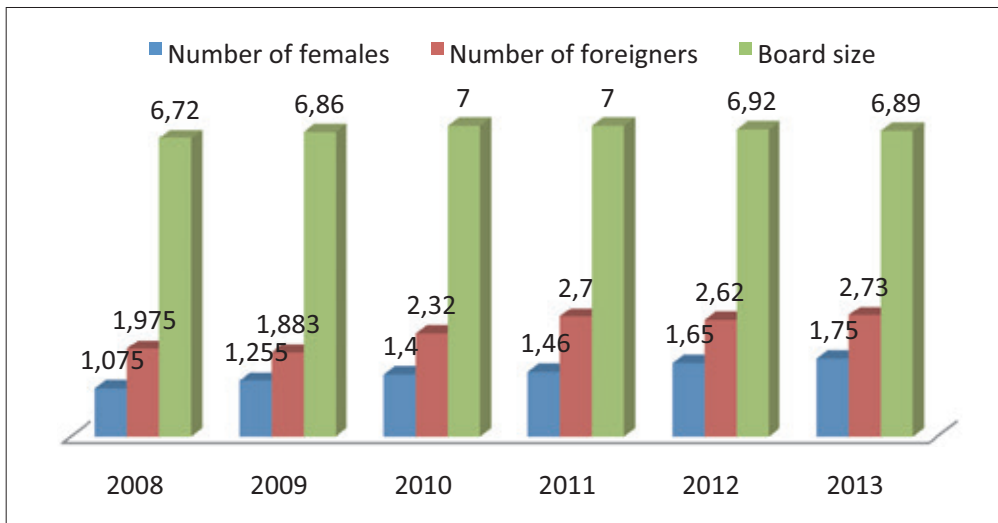


Figure 2. Board size and diversity

directors' personal characteristics (such as age and time served on the board) has also remained quite stable.

### 3.2 Univariate Tests

Companies with different nomination procedures differ in several respects. Table 3 presents mean values of key variables for companies with an internal nomination committee, as well as for companies with an external nomination committee composed of a group of experts.

The results from the difference-in-means tests indicate that boards whose candidates are chosen by an internal nomination committee (composed of board members) are more diverse in terms of director nationality, age diversity, and diversity in time served on the board of board members (See Table 3). Companies with an external nomination committee have more females and fewer independent directors on their boards, and they change their board members more often. These differences in board diversity are statistically sig-

Table 3. Difference-of-Means Test

VARIABLE	COMPANIES WITH INTERNAL TYPE OF NC	COMPANIES WITH EXTERNAL TYPE OF NC	DIFFERENCE	T-STATS
	N=188	N=140		
	NC-DUMMY=0	NC-DUMMY=1		
<b>BOARD DIVERSITY</b>				
Number of females	1.308	1.7	-0.4***	-3.65
% females	0.185	0.24	-0.052***	3.64
Female dummy	0.861	0.857	0.004	0.11
Number of foreigners	2.64	2.16	2.00**	2
% foreigners	0.367	0.3	0.067**	2.06
Foreign dummy	0.79	0.64	0.15***	3.12
Age dispersion	7.74	6.66	1.08***	3.8
Dispersion of time served on board	4.3	3.68	0.623**	2.39
<b>BOARD COMPOSITION</b>				
Board size	6.86	6.98	-1.2	-0.78
Av. director age	55.11	55.3	-0.004	-0.01
Av. time on board	5.35	4.43	0.92***	4
% independent	0.85	0.8	0.05**	2.29
<b>BOARD TURNOVER</b>				
Number of new directors	1	1.2	-0.2*	-1.654
Board renewal	0.14	0.165	-0.024	-1.4
Ownership				
Dual class shares	0.2	0.15	0.8**	1.78
% voting largest owner	0.13	0.22	-0.095***	-6.17
% voting second largest owner	0.059	0.079	-0.02***	-4.16
% voting third largest owner	0.04	0.05	-0.005*	-1.68
Voting rights of the five largest owners (sum)	0.27	0.39	-0.12***	6.71
<b>COMPANY CHARACTERISTICS</b>				
Assets	2759	3049	-290.3	-0.44
Leverage	0.251	0.292	-0.041**	-2.58
Lag ROA	4.4	1.28	3.15***	3.2
Lag net income	111.66	95.37	16.29	0.026

Note: This table reports the mean values of key board, ownership and company characteristics for companies with an internal type of Nomination committee and for companies with an external type of nomination committee. Mean differences are reported in the third column and \*, \*\*, \*\*\* denote statistical significance at the 10%, 5% and 1% levels respectively. t-statistics are reported in the last column

nificant, and they hold even where there are no statistically significant differences in board size that would make larger boards easier to diversify, or differences in board renewal where diversity would be the result of director replacement.

It can be seen that the ownership of companies with an external nomination committee is significantly more concentrated, whereas dual class shares are more prevalent among companies with an internal nomination committee. Compa-

nies with an external nomination committee tend to have more leverage and exhibit worse performance, both in terms of ROA and net income.

To summarise, differences in board diversity can be observed, depending on the type of nomination committee used. However, these differences alone are not enough to suggest that the type of nomination committee used has an impact on diversity. A number of other factors may influence board diversity. A multivariate analysis is used to further analyse the relationship between the type of nomination committee used and board diversity.

## 4. Multivariate Analysis

### 4.1 Nomination Committee and Board Diversity

Univariate tests show that companies with an internal nomination committee have more diverse boards, in terms of director nationality, age, and time served on the board, whereas companies with external nomination committees generally have more females on their boards. For a better understanding of whether these differences are the result of the type of nomination committee used or of underlying company characteristics unrelated to the procedure for selecting board member candidates, regression analyses are run with different aspects of diversity as dependent variables and the type of nomination committee as the key explanatory variable.

The relationship between the type of nomination committee used (*NC-dummy*, which is the key explanatory variable) and differences in the number of females on the board (*female*), international representation (*foreign dummy*), age dispersion (*sd age*), and dispersion in time served on the board (*sd time on board*), which are the dependent variables, is documented. Each of these dependent variables represents a different aspect of board diversity. Companies with an external nomination committee can be expected to have directors with more diverse backgrounds in terms of gender,

nationality, age, and experience.

A set of regressions is run to analyse the relationship between the type of nomination procedure and gender diversity, international diversity, diversity in age of board members, and diversity in seniority in board positions. As control variables a measure of ownership concentration (*% voting rights of the largest owner*), *board size*, the average age of board members (*av. board age*), and the average time served on the board of directors (*av. time on board*), the proportion of directors who have served less than a year (*board renewal*), the proportion of independent directors (*% indep.*), the proportion of female and foreign directors (*% female* and *% foreign*, respectively), ROA lagged one period, the log of total assets (*log assets*), and the ratio of total debt to total assets (*leverage*) are included. The results of these regressions are presented in Table 4.

Each column in Table 4 presents the results of an OLS regression with standard errors clustered by company. Each regression has a different dependent variable defining different aspects of board diversity. In columns (1) and (2) the dependent variable is the number of female directors on the board (*females*). In columns (3) and (4) the dependent variable is a dummy that takes the value one if at least one board member is not Finnish (*foreign dummy*). In columns (5) and (6) the dependent variable is the standard deviation of directors' age (*sd age*), and in columns (7) and (8) the dependent variable is the dispersion of directors' time on board (*sd time on board*).

**Gender diversity** is measured by the number of females on the board. It can be seen from Table 4, column 1 that companies with an external nomination committee hire 5% more female directors than companies with a nomination committee composed of board members. However, this difference becomes insignificant when ownership concentration is included in the regression equation (Table 4, column 2). In this case the percentage of voting rights of the largest owner is positively related to the number of female board members, irrespective of the type of nomination committee proposing director candidates. Company size

Table 4. Regression Results. NC and board diversity

Dep. Var.	GENDER DIVERSITY		DEMOGRAPHIC DIVERSITY		AGE DIVERSITY		TIME ON BOARD DIVERSITY	
	(1) Female	(2) Female	(3) Foreign dummy	(4) Foreign dummy	(5) Sd age	(6) Sd age	(7) Sd time	(8) Sd time
NC-External	0.05* (2.13)	0.025 (1.14)	-0.17* (-2.06)	-0.155* (-1.85)	-1.09* (-1.79)	-0.829 (-1.3)	0.66 (-1.36)	-0.788* (-1.72)
% voting largest owner		0.253*** (4.60)		-0.12 (-0.46)		-0.463 (-0.36)		2.71 (1.44)
Board size	-0.01 (-1.0)	-0.01 (-0.97)	0.004 (0.13)	-0.001 (0.05)	0.288 (1.62)	0.276 (1.47)	0.055 (0.32)	.063 (0.37)
Av. Board age	0.000 (0.23)	0.003 (1.27)	0.013 (0.96)	-0.0013 (-0.10)			-0.08 (-1.16)	-0.03 (-0.48)
Av. Time on board	-0.002 (-0.5)	-0.005 (-0.99)	-0.014 (-0.72)	0.008 (0.45)	0.022 (0.816)	0.04 (0.44)		
Board Renewal	0.045 (0.94)	0.034 (0.76)	-0.128 (-0.98)	-0.047 (-0.42)	0.109 (0.09)	0.398 (0.33)	-1.3 (-1.62)	-1.38** (-1.81)
% Indep.	0.11* (1.73)	0.06 (1.13)	0.42* (1.84)	0.603*** (2.99)	-2.03 (-1.02)	-2.01 (-0.91)	-1.48 (-1.28)	-2.48** (-2.13)
% Female			0.054 (0.18)	0.373 (1.36)	1.09 (0.52)	0.304 (0.15)	-0.97 (-0.50)	-2.62 (-1.22)
% Foreign	-0.03 (-0.76)	-0.002 (-0.06)			0.166 (0.18)	0.12 (0.13)	-1.83** (-1.85)	-0.99 (-1.07)
Lag ROA	0.001 (0.97)	0.001 (0.80)	-0.00 (-0.31)	-0.001 (-0.54)	0.043 (0.014)	0.036* (1.98)	0.039** (2.09)	0.047*** (2.76)
Log assets	0.038*** (5.23)	0.033*** (4.64)	0.13*** (3.65)	0.136*** (4.02)	-0.387** (-2.19)	-0.254 (1.44)	-0.07 (-0.37)	-0.16 (-0.92)
Leverage	-0.01 (-0.12)	-0.043 (-0.54)	-0.0055 (-0.02)	0.063 (0.22)	1.62 (0.87)	1.29 (0.68)	1.12 (0.63)	0.98 (0.55)
Constant	-0.12 (-0.72)	-0.24 (-1.50)	-0.14 (-1.57)	-0.14 (-1.57)	9.1*** (4.62)	8.3*** (3.95)	10.8*** (2.73)	9.15 (2.45)
N	323	323	323	304	285	266	323	304
Adjusted R-squared	0.3061	0.3799	0.4260	0.4707	0.1197	0.0836	0.1595	0.1886

Note: this table reports OLS regression results with standard errors clustered by company. In columns (1) and (2) the dependent variable is the proportion of female directors on the board. In columns (3) and (4) the dependent variable is a dummy that takes the value one if at least one director is a foreigner. In columns (5) and (6) the dependent variable is the standard age deviation of the board members. In columns (7) and (8) the dependent variable is the standard deviation of the time served on the board of directors. \*, \*\*, \*\*\* denote statistical significance at the 10%, 5%, and 1% levels respectively. t-statistics are in parentheses.

is also significantly related to the proportion of women on the board. The proportion of women on the board is unrelated to board size or independence, as it also is to company performance. Including information concerning ownership on the regression increases the explanatory power of the model by 7%. In all, the model can explain 37.99% of variation in gender diversity among Finnish companies.

**International diversity** is measured using a dummy variable that takes the value one if the company has at least one international board member (*foreign dummy*). This dummy variable is taken, not the total number of foreign board members, following (Piekkari, Oxelheim and Randoy, 2013). These authors argue that admitting a foreigner to a board (the shift from a national to an international board) may result in a disrupt-

tion in board routines and activities, imposing as it does a change in language on other board members. This disruption is relevant when the first foreigner is introduced to the board, whereas the total number of foreign board members is less relevant. Regression results for the relationship between international boards and the type of nomination procedure used are presented in Table 4, columns 3 and 4. There is a negative and significant relationship between the use of an external nomination committee and board internationalisation, but, as in the case of gender diversity, this relationship becomes insignificant (at a 5% level of significance) when ownership is included in the regression. The regression results indicate that external nomination committees might have a (marginally significant) preference for national board candidates.

A negative correlation between age and tenure of board members with company internationalisation, as suggested by Piekari *et al.*, is not found. However, larger companies and companies with more independent boards are more likely to have international boards. Up to 47% of the variation in internationalisation can be explained by the model.

**Diversity in terms of age and time served in directors' roles** can be important because these personal characteristics determine the relative position of directors on the board. Directors of different generations may have discrepancies of opinion and degrees of risk aversion; they differ in their overall experience and know-how; and they may disagree concerning the company's future growth. Age is, together with gender, one of the most important in-group aspects of social concentration. Yet, as in the case of gender diversity, the relationship between age dispersion and the type of nomination committee becomes non-significant when ownership concentration is included in the regressions.

There is no evidence to suggest that companies with an internal nomination committee have more cohesive boards (in terms of age) than those with an external nomination committee. On the contrary, Table 4, column (4) indicates that there is a negative relationship between external nomi-

nation committee use and age dispersion among board members. When ownership concentration is included in the analysis, this difference becomes insignificant, even when the largest owners' share of voting rights is unrelated to board members' age dispersion.

Finally, the relationship between the type of nomination committee and dispersion of time served on the board of directors is explored. Differences in director experience are relevant, because they may have an impact on the relative power of directors within the board. Longer serving directors have more access to information and insider knowledge than newly appointed directors, and may have accumulated power in the years they have served on the board. Less diversity in terms of tenure on a board of directors may result in a more balanced board in terms of individual directors' relative power.

In Table 4, columns 7 and 8 the dispersion of time served on the board is found to be lower for companies with an external nomination committee. This may be related to the fact that the average time served on the board of directors is lower when the nomination committee is composed of a group of experts, or it may simply reflect external experts' preference for homogeneous boards. However, this difference is marginal both in terms of magnitude and significance.

The results do not support social concentration theories, which suggest that incumbent board members prefer peers who share similar social and demographic profiles. There is no significant evidence suggesting that boards whose candidates have been chosen by a nomination committee composed of outside experts are more diverse than boards whose candidates are chosen by a committee composed of directors. If anything, the results suggest the opposite. There is a marginal negative relationship between the existence of a board-external nomination committee and the presence of foreign directors or the dispersion of time served in the role of board members. However, because of the small range of the coefficients and the statistics' low significance level, the conclusion is that there are no significant differences

in the board diversity of companies with these kinds of nomination procedure.

#### 4.2 Nomination Committee and Board Composition

In this section the effects of the type of nomination procedure used, not only on board diversity, but also on overall board composition, are analysed.

For the analysis, different OLS regressions with standard errors clustered by company are run. Reports for these regressions are presented in Table 5. As in the previous section, the different columns have different dependent variables, each of them measuring different aspects of board composition. The dependent variables are the size of the board in columns (1) and (2); the average board age in columns (3) and (4); the ratio of independent directors to board size in columns (5) and (6); and the average time served on the board of directors in columns (7) and (8).

From these regressions it can be seen that neither the type of nomination committee used, nor the largest owner's voting power, is significantly related to board composition measured by the number of board members (Table 5, columns 1 and 2), the average age of board members (Table 5, columns 3 and 4), and the ratio of independent directors to board members (Table 5 columns 5 and 6).

There is, however, a negative and significant relationship between the average time served on the board of directors and the type of nomination committee used. The average time served by board members is more than six months less for companies with an external nomination committee. This negative effect persists even when ownership concentration, return on assets, board characteristics, and leverage are controlled for. However, as previously with diversity of time served, this relationship is only marginally significant, and does not lead to the conclusion that different types of nomination committees are related to boards with different compositions.

### 5. Robustness Tests

To check the robustness of the results, a battery of sensitivity analyses, including different measures of dispersion, ownership, and alternative econometric techniques, is used. Additionally, the results from Table 4 have been replicated excluding state owned companies from the analysis. Sensitivity analyses are reported in tables 6, 7 and 8.

The results are robust to different measures of board diversity (for example, the proportion of females and non-national directors on the board) and to different measures of ownership. Results do not vary significantly when the voting rights of the three largest owners separately, or the sum of voting rights of the five largest owners, is included.

When panel data techniques (random effects estimators) are used, the relationship between the type of committee used and different measures of diversity becomes non-significant. This result reinforces the previous conclusion that the kind of nomination committee used has a limited impact on board diversity. Because of the small variation of corporate governance measures during the years of the sample (especially in the type of nomination committee used), random effects estimators may be less reliable than cross sectional regressions with cluster standard error. For this reason, the results from cross sectional regressions with cluster standard errors are reported as the main results.

State owned companies are excluded from the analysis in Table 8. Companies under state influence have a target of 40% of women on their boards, and state owned companies always adopt an external type of nomination committee. To avoid the bias that this positive correlation might bring to our main results, observations where the Finnish state is a block holder are excluded from Table 8. In all, there are twelve companies in the data, where the Finnish state is a block holder. Results are robust to the exclusion of those companies. The relation between the use of external nomination committee and board dispersion is ei-

Table 5. Regression Results. NC and board composition

DEP. VAR.	(1) BOARD SIZE	(2) BOARD SIZE	(3) AV. BOARD AGE	(4) AV. BOARD AGE	(5) % INDEP.	(6) % INDEP.	(7) TIME ON BOARD	(8) TIME ON BOARD
NC-External	0.078 (0.34)	0.084 (0.33)	-0.041 (-0.06)	0.12 (0.18)	-0.049 (-1.11)	-0.045 (-0.95)	-0.665* (-1.85)	-0.681* (-1.87)
% voting largest owner		0.39 (0.44)		-1.4 (-0.75)		-0.037 (-0.25)		0.93 (0.7)
Board size			0.043 (0.19)	-0.023 (-0.11)	-0.02 (-1.55)	-0.014 (-1.25)	-0.004 (-0.03)	0.015 (0.12)
Av. Board age	0.006 (0.19)	-0.03 (-0.11)			-0.008 (-1.21)	-0.000 (-0.15)	0.04 (0.61)	0.085 (1.33)
Av. Board Time in Role	-0.001 (-0.003)	0.006 (0.05)	0.104 (0.65)	0.222 (1.54)	-0.000 (-0.09)	-0.01 (-0.091)		
Board Renewal	0.399 (0.87)	0.465 (0.95)	-2.74** (-2.33)	-2.06* (-1.81)	-0.129 (-1.6)	-0.163** (-2.0)	-5.08*** (-8.64)	-5.01*** (-9.12)
% Indep.	-0.769 (-1.43)	-0.607 (-1.13)	-2.06 (-1.22)	-0.239 (-0.15)			-0.1 (-0.09)	
% Female	-0.798 (-1.03)	-0.89 (-1.02)	0.537 (0.23)	2.88 (1.3)	0.122 (1.53)	0.162 (1.09)	-0.721 (-0.52)	-1.68 (-1.11)
% Foreign	0.307 (0.82)	0.207 (0.53)	2.04 (1.4)	0.694 (0.49)	0.280 (1.6)	0.188** (2.57)	-0.61 (-0.80)	0.168 (0.25)
Lag ROA	-0.026*** (-3.62)	-0.029*** (-3.8)	-0.039 (-1.08)	-0.044 (-1.2)	-0.000 (-0.31)	0.000 (0.33)	0.43*** (2.91)	0.052*** (3.54)
Log assets	0.543*** (6.4)	0.57*** (6.14)	0.745*** (3.41)	0.77*** (3.92)	0.018 (1.06)	0.008 (0.5)	-0.056 (-0.34)	-0.144 (-0.94)
Leverage	-2.20** (-2.55)	-2.53** (-2.55)	-2.49 (-1.03)	-2.08 (-0.87)	-0.128 (-0.98)	-0.107 (-0.83)	-0.481 (-0.32)	-0.5 (-0.32)
Constant	4.25*** (2.6)	4.45** (2.62)	51.73*** (23.72)	49.8*** (24.65)	1.24*** (4.35)	0.958*** (3.52)	4.65 (1.38)	3.19 (1)
N	323	304	323	304	323	304	323	304
R-squared	0.4290	0.4250	0.2386	0.2402	0.1326	0.1572	0.2653	0.3083

Note: this table reports OLS regression results with standard errors clustered by company. In columns (1) and (2) the dependent variable is the board size. In columns (3) and (4) the dependent variable is the average age of board members. In columns (5) and (6) the dependent variable is the ratio of independent directors to board size. Independent directors are defined as those who are independent from management and largest shareholders. In columns (7) and (8) the dependent variable is the average time served on the board of directors. \*, \*\*, \*\*\* denote statistical significance at the 10%, 5%, and 1% levels respectively. t-statistics are in parentheses.

Table 6. Robustness test. Alternative measures of ownership

Dep. Var.	GENDER DIVERSITY		DEMOGRAPHIC DIVERSITY		AGE DIVERSITY		TIME ON BOARD DIVERSITY	
	(1) Female	(2) Female	(3) Foreign d.	(4) Foreign d.	(5) Sd age	(6) Sd age	(7) Sd time	(8) Sd time
NC-External	0.023 (-1.08)	0.03 (-1.41)	-0.154* (-1.83)	-0.159* (-1.89)	-1.008 (-1.51)	-0.993 (-1.54)	-0.986** (2.21)	-0.822* (-1.86)
% voting of five largest shareholders (sum of votes)	0.207*** (4.17)		-0.102 (-0.42)		1.441 (-0.78)		4.033*** (2.68)	
% voting largest owner		0.244*** (4.49)		-0.119 (-0.45)		-0.015 (-0.01)		2.393 (-1.45)
% voting second largest owner		-0.346 (-1.22)		0.255 (-0.34)		3.883 (-0.65)		-0.592 (-0.17)
% voting third largest owner		0.955** (2.27)		-0.645 (-0.42)		14.686 (-1.17)		28.331*** (2.89)
Board size	-0.006 (-0.78)	-0.009 (-1.17)	-0.003 (-0.09)	-0.001 (-0.04)	0.257 -1.31	0.266 (-1.42)	0.084 (-0.53)	0.076 (-0.5)
Av. Board age	0.004 (-1.43)	0.004 (-1.39)	-0.002 (-0.14)	-0.002 (-0.13)			-0.021 (-0.32)	-0.017 (-0.24)
Av. Time on board	-0.008 (-1.38)	-0.008 (-1.4)	0.01 (-0.53)	0.01 (-0.53)	0.024 (-0.26)	-0.018 (-0.19)		
Board Renewal	0.025 (-0.57)	0.016 (-0.36)	-0.042 (-0.39)	-0.036 (-0.35)	0.252 (-0.21)	-0.094 (-0.08)	-1.358* (-1.9)	-1.421** (2.01)
% Indep.	0.057 (-1.01)	0.035 (-0.71)	0.606*** (3.01)	0.617*** (2.97)	-1.765 (-0.78)	-1.79 (-0.77)	-2.46** (2.14)	-2.849** (2.43)
% Female		0.397 (-1.43)	0.376 (-1.3)	-0.343 (-0.15)	-0.453 (-0.21)	-3.396* (-1.79)	-3.288* (-1.65)	
% Foreign	-0.005 (-0.11)	0.004 (-0.1)			0.183 (-0.2)	0.275 (-0.32)	-1.073 (-1.2)	-0.995 (-1.13)
Lag ROA	0.001 (-1.07)	0.001 (-0.82)	-0.003 (-0.63)	-0.002 (-0.61)	0.037* (-1.94)	0.039** (2.18)	0.046** (2.54)	0.042** (2.19)
Log assets	0.035*** (4.81)	0.037*** (5.26)	0.136*** (3.97)	0.134*** (3.87)	-0.213 (-1.11)	-0.12 (-0.56)	-0.128 (-0.74)	-0.023 (-0.13)
Leverage	-0.044 (-0.54)	-0.057 (-0.75)	0.055 (-0.19)	0.065 (-0.22)	0.92 (-0.47)	0.527 (-0.26)	0.872 (-0.52)	0.477 (-0.31)
Constant	-0.303* (-1.82)	-0.262 (-1.58)	-0.589 (-0.84)	-0.601 (-0.83)	7.8*** (3.54)	6.874*** (2.78)	7.567** (2.15)	6.612* (-1.75)
N	304	304	304	304	266	266	304	304
Adjusted R-squared	0.35	0.37	0.45	0.45	0.05	0.08	0.21	0.25

Note: this table reports OLS regression results with standard errors clustered by company. In columns (1) and (2) the dependent variable is the proportion of female directors on the board. In columns (3) and (4) the dependent variable is a dummy that takes the value one if at least one director is a foreigner. In columns (5) and (6) the dependent variable is the standard age deviation of board members. In columns (7) and (8) the dependent variable is the standard deviation of time served on the board of directors. \*, \*\*, \*\*\* denote statistical significance at the 10%, 5%, and 1% levels respectively. t-statistics are in parentheses.



Table 7. Robustness Test. Random effect estimator

RANDOM EFFECT ESTIMATOR	GENDER DIVERSITY	DEMOGRAPHIC DIVERSITY	AGE DIVERSITY	DIVERSITY OF TIME SERVED ON BOARD
DEPENDENT VARIABLE	(1) FEMALE	(2) FOREIGN D.	(3) SD AGE	(4) SD TIME
NC-External	0.011 (-0.56)	-0.071 (-1.23)	-0.169 (-0.31)	-0.654 (-1.61)
% voting largest owner	0.221*** (3.34)	-0.108 (-0.63)	-2.784* (-1.69)	0.909 (-0.72)
Lag ROA	-0.001 (-0.77)	-0.003 (-1.63)	0.005 (-0.3)	0.005 (-0.41)
Board size	-0.009 (-1.43)	0.043*** (3.34)	0.255** (2.01)	0.154 (-1.55)
Av. Board age	0.001 (-0.31)	0.006 (-1.23)		0.04 (-1.03)
Av. Time in role	-0.006 (-1.48)	-0.018** (1.99)	0.138 (-1.6)	
Board renewal	0.002 (-0.05)	-0.035 (-0.54)	0.876 (-1.28)	0.363 (-0.76)
Log assets	0.038*** (5.10)	0.103*** (4.28)	-0.3 (-1.51)	-0.249 (-1.52)
Leverage	-0.074 (-1.29)	-0.002 (-0.02)	1.459 (-1.2)	0.329 (-0.35)
% Indep.	0.049 (-1.13)	0.244*** (2.66)	1.062 (-1.14)	-0.073 (-0.1)
% Foreign	-0.017 (-0.49)		-0.484 (-0.58)	-1.575** (2.29)
% Female		-0.028 (-0.25)	-0.359 (-0.31)	-0.849 (-0.99)
Constant	-0.051 (-0.37)	-0.631** (2.03)	6.206*** (3.85)	3.198 (-1.39)
Observations	304	304	266	304
N of companies	62	62	55	62

Note: Random effects estimation. In column (1) the dependent variable is the proportion of female directors on the board. In column (2) the dependent variable is a dummy that takes the value one if at least one director is a foreigner. In column (3) the dependent variable is the standard age deviation of board members. In column (4) the dependent variable is the standard deviation of time served on the board of directors. Absolute value of z-statistics are in parentheses. . \*, \*\*, \*\*\* denote statistical significance at the 10%, 5%, and 1% levels respectively. t-statistics are in parentheses

Table 8. Regression Results. NC and board diversity excluding stated owned companies

DEP. VAR.	GENDER DIVERSITY		DEMOGRAPHIC DIVERSITY		AGE DIVERSITY		TIME ON BOARD DIVERSITY	
	(1) FEMALE	(2) FEMALE	(3) FOREIGN DUMMY	(4) FOREIGN DUMMY	(5) SD AGE	(6) SD AGE	(7) SD TIME	(8) SD TIME
NC-External	0.005* (0.185)	-0.004* (-0.173)	-0.214** (-2.015)	-0.207** (-2.000)	-1.293** (-2.001)	-1.038 (-1.490)	-0.042 (-0.072)	-0.260 (-0.466)
% voting		0.18*** (2.694)		-0.139 (-0.421)		0.47** (0.238)		5.35** (2.196)
largest owner								
Board size	0.000 (0.005)	0.000 (-0.030)	-0.004 (-0.100)	-0.015 (-0.417)	0.206 (0.926)	0.176 (0.721)	0.064 (0.355)	0.061 (0.333)
Av. Board age	-0.003 (-0.692)	0.001 (0.312)	0.013 (0.788)	-0.005 (-0.347)			-0.053 (-0.775)	-0.007 (-0.102)
Av. Time on board	0.003 (0.525)	-0.001 (-0.176)	-0.009 (-0.443)	0.016 (0.894)	0.023 (0.236)	0.036 (0.367)		
Board Renewal	0.077 (1.357)	0.069 (1.348)	-0.221 (-1.494)	-0.131 (-1.073)	-0.262 (-0.170)	0.084 (0.052)	-1.349 (-1.278)	-1.517 (-1.551)
% Indep.	0.088 (1.610)	0.023 (0.445)	0.44* (1.809)	0.7*** (3.502)	-2.885 (-1.271)	-2.793 (-1.080)	-1.496 (-1.270)	-2.8** (-2.334)
% Female			-0.099 (-0.230)	0.327 (0.852)	2.103 (0.725)	0.787 (0.282)	1.868 (0.710)	-0.364 (-0.127)
% Foreign	-0.014 (-0.344)	0.020 (0.468)			0.124 (0.126)	0.117 (0.122)	-2.2** (-2.043)	-1.312 (-1.296)
Lag ROA	0.001 (0.528)	0.000 (0.433)	-0.001 (-0.181)	-0.002 (-0.378)	0.04** (2.214)	0.033 (1.587)	0.05*** (2.663)	0.05*** (2.853)
Log assets	0.03*** (3.937)	0.02*** (3.530)	0.1*** (3.529)	0.14*** (3.889)	-0.39* (-1.845)	-0.224 (-0.975)	-0.011 (-0.054)	-0.063 (-0.320)
Leverage	-0.055 (-0.642)	-0.100 (-1.242)	-0.030 (-0.086)	0.108 (0.318)	1.415 (0.604)	0.711 (0.283)	1.886 (0.990)	1.465 (0.692)
Constant	0.064 (0.326)	-0.065 (-0.361)	-1.028 (-1.287)	-0.448 (-0.594)	10.3*** (4.472)	9.5*** (3.701)	8.2** (2.161)	6.6* (1.903)
N	263	244	263	244	225	206	263	244
Ad R-squared	0.1660	0.2024	0.4051	0.4639	0.0805	0.0284	0.1206	0.1697

Note: This table replicates the analysis on Table 4, excluding those observations where the state is one of the block holders. This table reports OLS regression results with standard errors clustered by company. In columns (1) and (2) the dependent variable is the proportion of female directors on the board. In columns (3) and (4) the dependent variable is a dummy that takes the value one if at least one director is a foreigner. In columns (5) and (6) the dependent variable is the standard age deviation of the board members. In columns (7) and (8) the dependent variable is the standard deviation of the time served on the board of directors. \*, \*\*, \*\*\* denote statistical significance at the 10%, 5%, and 1% levels respectively. t-statistics are in parentheses

ther not statistically significant (table 8, columns 6 and 8) or negative and significant (table 8, columns 2 and 4). Thus, one cannot observe that companies with internal nomination committees have a less diverse board than those where shareholders actively engage in the nomination of candidates through an external nomination committee.

In all our results are not in line with the argument that members of internal nomination committees might use their influence to achieve a more homogeneous board. The use of external nomination committee to counteract this preference might prove thus to be redundant.

## 6. Conclusions

The active engagement of large shareholders is a key feature of the Nordic Model of Corporate Governance. This engagement is especially important in companies where the largest shareholders are entitled to influence the selection of director candidates via the direct appointment of nomination committee members. The extensive decision making authority assigned to the board of directors in Nordic Countries gives a great deal of control over their companies to these largest shareholders.

In this study the extent to which this power to select director candidates leads to relevant differences in terms of board diversity or composition is analysed. Using data on Finnish companies between 2008 and 2013, the characteristics of boards of directors in companies where board candidates are selected directly by the largest shareholders, as opposed to boards where director candidates are selected by a nomination committee composed of board members, are compared.

Companies with an external nomination committee (directly appointed by the largest shareholders) are generally found to have more female directors on their boards, but are less diverse demographically, and in terms of age dispersion and time served on the board of their directors. Controlling for ownership, governance, and company characteristics, only marginally significant

differences in demographic diversity and time served persist. No significant difference in terms of board size, independence, and average age or experience of board members is found. Hence, the results suggest that – once ownership structure is taken into account – the procedure for selecting director candidates has a limited impact on final board composition.

These results are especially relevant, as they do not support the widely held belief that allowing incumbent directors to select director candidates is detrimental to companies. Critics argue that incumbent directors may not choose candidates of more merit or who are better equipped to serve on the board, but may opt instead for lesser qualified candidates who will not threaten incumbent members' positions, and who make their board work easier. If that were the case, one should expect to observe less diverse boards when nomination committees are composed of board members.

However, the results suggest – if anything – the opposite. There is no evidence to suggest that incumbent directors on nomination committees use their position to promote socially homogeneous boards. Directors' screening of the initial pool of candidates (through a board-internal nomination committee) does not lead to significant differences in board composition, in gender, or age diversity. When unobserved heterogeneity is controlled for using random effects estimators, the kind of nomination committee used is non-significantly related to any measure of board dispersion.

These results are important at the European level, as the harmonisation of corporate governance standards at EU level has posed a challenge to the Nordic corporate governance model. The model (that of strong owners and powerful boards *vis à vis* management teams) has been modified with the introduction of codes that shift the accent from strong monitoring owners to independent boards with more formal internal working procedures. One such formal working procedure is to establish an internal nomination committee, where incumbent board members select potential candidates. The results suggest that this shift, despite the changes in formal procedure, does not

significantly alter the final board composition.

The results are also relevant outside Europe. Bank of America, the second largest bank in the United States, has changed its bylaws to allow long-term investors to nominate directors to the board. Other companies, such as General Electric and Prudential Financial Inc., have followed this shift towards a shareholder friendly nomination process, known in the US as “proxy access”. In the UK the Tomorrows Company, a business-led think tank, promotes the active engagement of shareholders in the nomination process, through the use of “Swedish-Style Nomination Committees”. The results of this study suggest that, with adequate monitoring of shareholders, internal nomination committees do not use their power

to select candidates differently than do external nomination experts, and external nomination committees do not outperform internal committees in selecting director candidates.

When actively choosing director candidates, large shareholders have to address the question of what they would do differently than internal nomination committees. What is their comparative advantage with respect to incumbent board members in choosing candidates? When are external nomination committees preferred to shareholders directly presenting their candidates at the Annual General Meeting? Only when these questions are fully addressed can the kind of nomination committee have a clear impact on the actual composition of the board.

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