This study examines the factors that influenced the number of new boards joined by directors of the largest U.S. corporations in 1982. Social connections had by far the greatest impact on joining new boards, while the performance of the firms on whose boards directors sat had little discernible effect.

Substantial research has documented the existence of an interlocking directorate network linking virtually all large American corporations into a single social structure through shared board memberships (Mints and Schwartz, 1985). Two firms are said to interlock when one or more individuals sit on both of their boards of directors. The median Fortune 500 firm in 1986 shared directorships with seven other large firms, indicating the pervasiveness of interlocks. Moreover, several studies in the past few years have documented that shared directorates act to influence top management salaries (O'Reilly, Hall, and Crystal, 1985) and to spread organizational structure (Palmer, Jennings, and Zhou, 1992), strategies to defend against takeovers (Dove, 1991), and political strategies (Kissell, 1982). Thus, interlocks are both pervasive and extremely significant, providing an influential social context for corporate governance. But while researchers have focused on the organizational purposes that may be served by sharing a director with a particular firm—cooperation in a supply line, or dilution of a resource or lobbying of a dependent firm—we have little systematic evidence on how individuals come to serve on multiple boards. Yet the question of how individuals become central in the network is of considerable theoretical and practical importance, as these individuals are the raw material of the intercorporate network.

The market for directors can be analyzed like other labor markets. Joining new boards is the only recognized form of promotion among directors. If a new board is regarded by this market. Thus, directors who get invited to join additional boards and why indicates what the political economy of the network rewards. Moreover, becoming a multiple director is the gateway to serving on business policy organizations and governmental advisory boards, as demonstrated by the marked differences in participation on these bodies between directors of single and multiple boards (Hansen, 1981).

The board of directors is elected by the shareholders to represent their interests in the corporation. In particular, the board functions to monitor top management—selecting managers, setting their salaries, and firing them if necessary—and to ratify important decisions. Thus, an examination of the way in which boards are appointed can highlight the shareholders’ role in the selection process and shed light on how shareholders control the corporation. In particular, the way in which boards are appointed can highlight the shareholders’ role in the selection process and shed light on how shareholders control the corporation.

The question of whose interests are served by boards can be approached by studying who gets ahead in the corporate director labor market. The market for directors is like the market for marriage partners; potential board members have
Agency theory

Agency theorists argue that the human capital of directors is in part determined by the performance of the firm with which they are associated (Fama and Jensen, 1983). In this view, the market for directors rewards directors whose firms are better performers. Firms looking for new directors should most sensibly seek directors of firms that have done well in the past.

H1: Directors of better-performing firms will join more new boards than directors of poorer performers.

membership on the board of a firm that becomes a takeover target is a particularly strong signal that can affect membership on new boards. Fama and Jensen (1983: 315) argue that "there is substantial dissolution of human capital when internal decision control breaks down and the costly last resort process of an outside takeover is activated." Therefore:

H2: Directors of hostile takeover targets will join more new boards than directors of non-targets.

Managerialism

While agency theory focuses on the role of board members as agents of shareholder interests, managerialist theorists have focused on the board as a social institution. The ability to serve shareholders takes a back seat to social connections and the ability to serve managerial interests in this view. Social connections serve a critical role in labor market mobility, and in general, close connections lead to greater mobility (Granovetter, 1985). Anecdotal evidence suggests that this is true in the market for directors as well. (Queen, 1982: 10) finds that "personal connections to join a particular company board...tend to move along the networks of personal friendship and personal connections." In particular, serving on one firm's board with the chairman or other director of another firm is a common source of invitations to join the other firm's board. Thus, the social connections that come from sitting on multiple boards should lead to more invitations to join additional boards. Furthermore, sitting on the board of a firm that is central in the interlock network (that is, a firm whose directors sit on numerous other boards) should also lead to more invitations to join additional boards.

H3: Directors that sit on multiple boards will join more new boards than directors that sit on one board.

H4: Directors of firms that are more central in the interlock network will join more new boards than directors of less central firms.

In addition to social connections, directors can get ahead through compliance with top management. To the extent that invitations to join the board come from the CEO, one should expect that directors from boards with a history of serving management interests would be more appealing candidates than directors that have opposed management.

H5: More compliant directors will join more new boards than less compliant directors.

A final appealing feature of a director from the point of view of top management is the ability to defend the firm against outside threats. The most prominent threat during the 1980s was that posed by hostile takeovers. A large number of firms faced unwanted takeovers during the study period, and directors that demonstrated their ability to fend off takeovers should have been particularly attractive candidates from management's perspective.

H6: Directors of firms that were successfully defended against hostile takeovers will join more new boards than those that were not.

Bank Control Theory

The final hypothesis comes from bank control theory, which argues that banks play a particularly crucial role in the intercorporate network by virtue of their control over capital flows (Fama, 1970). Bank power is exercised both through ownership and through placing representatives on the boards of subject firms to assure that these firms maintain profitability. Because we can use the proximity to role commercial banks play in the economy, they have been particularly attractive candidates for company boards. Thus:

H7: Bank executives will join more new boards than other directors.

Because directors of larger firms are likely to be more visible on the market for directors, I controlled for firm size using total assets.

DATA

The initial sample for this study included all directors that sat on the boards of firms in either the 1980 or 1985 Fortune 500 largest...
industries in the 50 largest commercial banks, 25 largest financial service firms, 25 largest retailers, or 25 largest transportation firms during 1982. 625 individuals occupied 8425 board memberships on the boards of the 500 largest firms in this universe for which data were available.

Board data for the sampled firms were collected for 1980, 1984, and 1990. Due primarily to mergers and takeovers, the sample of firms dropped in size from 646 in 1980 to 522 in 1984 and to 456 by 1990. 1982 board data came from Standard and Poor's Directory of Corporations, directors, and executives. 1980 and 1990 board data came from Compustat Disclosure. I used several techniques to ensure the quality of the data and its comparability across years, including numerous computerized routines and hand-checks. For each of the three good years I calculated the number of boards each director sat on as a measure of individual network centrality. It also determined which new boards (if any) each director sat in in 1984 and 1990. The dependent variable was calculated as the count of new board memberships in 1984 or 1990, finally. I noted a dummy variable for being an executive of a commercial bank.

firm centrality was measured for 1982 and 1986 as the number of unduplicated interlocks each firm had with other firms in this population—i.e., the number of other firms with which the focal firm shared at least one director. Directors were assigned a score for the mean centrality (number of interlocks) of the boards on which he/she served in 1982 and 1990.

Corporate performance and size data came from the firm's balance sheet. I used the four measures of performance, return on equity, which measured year-to-year performance, and each-to-year ratio, which measures the stock market's evaluation of the firm's long-term prospects. size was measured using total assets. Directors were assigned the average value of these measures over each of the firms on whose boards he/she sat.

Data on takeover attempts came from 1963 (strenthen offer filings reported in the SEC Wave Discourse for 1980-1990 and the COMPSTAT database for 1980-1990). Job offers to academics were those tender offers made by an outside party that were realized by the board of directors, according to reports in the Wall Street Journal. Directors were given count variables for the number of firms they were members of hostile takeover attempts between 1960 and 1989 (for the 1960-1989 analyses) and between 1986 and 1989 (for the 1986-1989 analyses). Directors were also given count variables for the number of hostile takeover attempts that they successfully funded off during the same periods. This is the number of hostile takeover attempts that ended with the firm maintaining independent rather than being acquired either by the original raider or by another acquirer.

I used two measures of director compliance. Most of the time adopted ‘golden parachute” contracts that compensated top managers if the firm was taken over. Golden parachutes were quite controversial during the 1980s—while managers found them appealing for obvious reasons, shareholders were less convinced, and some have argued that adopting a golden parachute is a good indicator of board compliance (e.g., Watts, O'Reilly, and Chandratat, 1970). “Poison pills” were also adopted by the boards with large shareholdings during the 1980s. Like parachutes, pills were quite controversial and generally perceived by opposition from shareholders because they put hostile takeover more difficult, thus potentially depleting shareholders of the premium that acquirers successfully take over (Davis 1991). Because both pills and parachutes are broadly favored by management but not by shareholders, sitting on boards that adopted these measures can be seen as a measure of director compliance. Thus, I created count variables for the number of boards on which a director sat that adopted parachutes and pills, respectively, between 1980 and 1989 (for the 1986-1989 analysis) and between 1986 and 1990 (for the 1986-1990 analysis). Data on the adoption dates of poison pills by firms in this population came from the Investor Responsibility Research Center (1982), while data on the adoption dates of golden parachutes came from IRRC and proxy statements.

METHOD

The dependent variable of interest was the number of new boards that directors joined. Because this is a count variable (i.e., only non-negative integers are possible values) and because the data are from the 1980s, I created non-negative integers are possible values) and because the data are from the 1980s, I created a new count variable for each firm-year. This variable is an indicator of the rate at which events (such as joining new boards) occur over a set of independent variables. The model takes the form

\[ C_{ij} = \exp(\beta' F) \]

where \( C_{ij} \) is the expected number of new board memberships, \( F \) is a vector of covariates, and \( \beta \) is a vector of coefficients. This model is disjunctive from the fact that it is log-linear. the effects of the covariates combine multiplicatively rather than additively. Exponentiating a coefficient gives the estimated multiplier effect that a one-unit change in the covariate has in the expected rate of new board memberships.

I estimated two models, one for the number of new board memberships attained between 1982 and 1989, and one for the period between 1989 and 1990. The model assumes that the number of new board memberships attained between 1982 and 1989 is independent rather than being acquired either by the original raider or by another acquirer.

I used two measures of director compliance. Most of the time adopted ‘golden parachute” contracts that compensated top managers if the firm was taken over. Golden parachutes were quite controversial during the 1980s—while managers found them appealing for obvious reasons, shareholders were less convinced, and some have argued that adopting a golden parachute is a good indicator of board compliance (e.g., Watts, O'Reilly, and Chandratat, 1970). “Poison pills” were also adopted by the boards with large shareholdings during the 1980s. Like parachutes, pills were quite controversial and generally perceived by opposition from shareholders because they put hostile takeover more difficult, thus potentially depleting shareholders of the premium that acquirers successfully take over (Davis 1991). Because both pills and parachutes are broadly favored by management but not by shareholders, sitting on boards that adopted these measures can be seen as a measure of director compliance. Thus, I created count variables for the number of boards on which a director sat that adopted parachutes and pills, respectively, between 1980 and 1989 (for the 1986-1989 analysis) and between 1986 and 1990 (for the 1986-1990 analysis). Data on the adoption dates of poison pills by firms in this population came from the Investor Responsibility Research Center (1982), while data on the adoption dates of golden parachutes came from IRRC and proxy statements.
required, and takeover attempts successfully defeated again between 1960 and 1964.

**RESULTS AND DISCUSSION**

The results, presented in Table 1, indicate that firm performance, as measured by mean ROE and market-to-book, had no discernible effect on subsequent board membership. Subsequent analyses using stock market returns also showed no significant effect. These null findings failed to support H1 from agency theory.

Surprisingly, the impact of hostile takeover attempts a director faced bore a positive and significant relation to the number of new board memberships held. This is quite contrary to H2, as well as to common sense. Further investigation suggested an explanation for the anomalous result: directors of target firms that were successfully taken over were often (although by means always) subsequently asked to sit on the board of the acquiring company, whether the acquirer was the bidder that originated the bid or a white knight. An empirical test of this hypothesis was designed. For example, two members of the Board of St. Regis in 1963, which faced hostile takeover in 1964 and was ultimately acquired by Champion International, ended up on Champion's board in 1961. An alternative test, in which the dependent variable was the total number of boards on which a person served rather than the number of new board memberships, indicated that, as expected, board membership of firms that faced hostile takeover subsequently sat on fewer boards, although surprisingly this effect was also significant for the 1963-1970 period.

As predicted by H3 and H4, directors that sat on more boards and directors of more central firms experienced significantly higher rates of new board memberships. An individual that sat on two boards in 1962 and joined the board of St. Regis in 1964 was almost certain to sit on only one board in 1970. Moreover, individuals that sat on the boards of firms that were subsequently taken over were substantially more likely to be asked to sit on additional boards than those that did not.

The results gave no support to H5, directors that sat on boards adopting golden parachutes between 1960 and 1969 subsequently joined new boards. Although there was a discernible trend in this direction for adoption of poison pills in either period or for poison pills over the period, this trend was not statistically significant. The results are broadly consistent with the notion that the director's market is segmented, so that the interests of those on the higher-tier boards are more highly priced by the director market, although the lack of correspondence across cutoffs suggests that caution in interpreting these results is warranted.

H6, that directors skilled at battling hostile takeover bids would be more likely to sit on boards that experienced a lower rate during the 1963-1984 period, although this effect was only marginally significant.

**REFERENCES**

The effect must be interpreted in light of the fact that the model controls for hostile bids received, which had a positive effect on new board memberships. Thus, for example, the two St. Regis directors that joined the board of Champion International would not have done so if St. Regis had avoided acquisition entirely.

Finally, there was no support for H7. Bank executives did not join boards at a higher rate than other directors in the 1963-1964 period, and joined at a significantly lower rate in the 1965-1970 period. This finding gives little reason to believe that bank executives occupied a privileged position in the interlock network.

**TABLE 1**

<table>
<thead>
<tr>
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<tbody>
<tr>
<td>Return on equity (ROE)</td>
<td>0.0290</td>
<td>0.0252</td>
</tr>
<tr>
<td>Market-to-book (M/B)</td>
<td>-0.0093</td>
<td>-0.0067</td>
</tr>
<tr>
<td>Quarterly turnover</td>
<td>-0.0212</td>
<td>-0.0590</td>
</tr>
<tr>
<td>Number of board memberships</td>
<td>0.0332</td>
<td>0.0332</td>
</tr>
<tr>
<td>Interlock networks</td>
<td>0.0152</td>
<td>0.0167</td>
</tr>
<tr>
<td>Controllability</td>
<td>0.5145</td>
<td>0.5145</td>
</tr>
<tr>
<td>Golden parachutes</td>
<td>0.0054</td>
<td>0.0054</td>
</tr>
<tr>
<td>Poison pills adopted</td>
<td>-0.0093</td>
<td>-0.0053</td>
</tr>
<tr>
<td>Successful acquisitions</td>
<td>-0.0495</td>
<td>-0.0495</td>
</tr>
<tr>
<td>Bank executive</td>
<td>0.0173</td>
<td>0.0173</td>
</tr>
<tr>
<td>Total assets</td>
<td>0.6000</td>
<td>0.6000</td>
</tr>
<tr>
<td>Sales</td>
<td>-0.0155</td>
<td>-0.0155</td>
</tr>
<tr>
<td>Intercepts</td>
<td>-3.3270</td>
<td>-3.3270</td>
</tr>
<tr>
<td>Chi</td>
<td>394.56</td>
<td>260.13</td>
</tr>
</tbody>
</table>

The results overall suggest that success in the market for directors is determined overwhelmingly by social connections and to some degree by compliance with management. Overall, it was not statistically significant for any director to be appointed to multiple new boards. However, the single most important variable was one that shared directors with a large number of other firms, which exposed one to more opportunities to be invited onto additional boards. While these results are entirely consistent with the idea of a network structure, they indicate that even at the top of the labor market, connections count for more than merit in determining advancement.

This conclusion must be tempered by the fact...
that this study only had access to corporate-level data. It is not that potential directors are evaluated not on the performance of the firm on whose boards they already sat but on some other criteria for merit such as educational background, such as attendance at elite universities, can be simply another proxy for social connections. Hence, it is reasonable to assume that corporate performance is a mere direct indicator of the capability of a director or personal characteristics.

This study is also limited by the fact that the self-assessment methods. The reported results only indicate broad tendencies in the market for directors and provide limitations in any particular case. More importantly, recent research in the literature on social influence and reputation has suggested that the results reported here are consistent with the general findings in the literature on social influence and reputation. However, it is important to note that the relationship between social influence and reputation is complex and depends on a variety of factors such as the nature of the network, the type of influence, and the context in which it occurs.

CONCLUSION

This study sought to determine how directors get ahead in the intercorporate network by assessing the factors influencing the number of new boards joined by large and comprehensive panel of directors between 1982 and 1992. I contrasted approaches that suggest different nurtures factors—agency theory, which argues that directors are rewarded for acting on the boards of successful firms, and a managerialist approach that sees directors playing a more active role in shaping the performance of the firm. By far the most important factors determining whether a director joined new boards was how many boards he/she already served on and how well-connected these boards were. As with other labor markets, social connections took precedence over demonstrated merit in determining success in the market for directors. There was also some support for the notion that directors were most likely to serve non-profit interests (by agreeing to golden parachutes) when advancement into the inner circle was possible.

This study provides the first systematic evidence on how directors move into the inner circle of the intercorporate network. The results indicate that the political economy of the network advantage directors that are connected and compliant, while directors that sit on the boards of poorly performing firms— even targets of hostile takeovers—are not punished. The market for directors does not reward vigilant agents or shareholder interests as hypothesized by agency theorists, but rather those best able to serve managerial interests as suggested by organization theorists in the managerialist tradition.

REFERENCES


