The Relationship of Board Member Diversity to Organizational Performance

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ABSTRACT. Wider diversity in board member characteristics has been advocated as a means of improving organizational performance by providing boards with new insights and perspectives. With data from 240 YMCA organizations, a board diversity index was constructed and compared to multiple measures of board member diversity. Results revealed higher levels of social performance and fundraising results when board members had greater occupational diversity. Gender diversity compared favorably to the organization's level of social performance but a negative association surfaced for level of funds raised. The diversity in board member age groupings was linked to higher levels of donations.

In board of director literature, a recurring theme is that board composition can impact organizational performance. In fact, research studies have revealed associations between board member characteristics and financial measures of organizational performance. For example, some researchers have equated the insider orientation of board members (close ties to management) with greater profitability (Cochran et al., 1985; Vance, 1978); others have focused on occupational characteristics of directors as important indicators of firm performance (Baysinger and Butler, 1985; Zald, 1967). Also, researchers have attempted to compare board size (Chaganti et al., 1985; Hiner, 1967; Pfeffer, 1973) and gender composition (Babchuk et al., 1960; Provan, 1980) to organizational performance. (See Zahra and Pearce 1989, for a complete review of the literature on boards of directors and company performance.)

Recently, the economic concern with defining the best composition of individual to direct and oversee a company's operation has been broadened to include a concern with corporate social performance and the participation of underrepresented groups (Fryxell and Lerner, 1989; Zahra and Stanton, 1988). While the issue of greater representation by a variety of board member types has been advocated to provide a diversity of outlook (Bere, 1991), few empirical studies have approached board composition from this diversity perspective.

The study reported here addresses this shortcoming and extends past research efforts in the area of board composition by developing a diversity index and investigating its relationship to both social and economic organizational performance.

Theoretical framework

The assumption that the selection of particular individual directors affects organizational performance can be traced to resource dependence theory (Aldrich, 1979; Pfeffer and Salancik, 1978). According to this framework, boards are part of the organization and its environment, and by providing information and resources to the organization, boards help to cushion it against an uncertain environment. This viewpoint suggests that on an individual basis, board members bring resources to the organization as a result of their backgrounds (Zald, 1969). In addition to the environmental linkage perspective, a second framework argues that board members perform an internal control function (Pfeffer, 1973; Zald, 1969), and through administrative efforts can influence organizational efficiency. Both viewpoints suggest that properly structured governing boards have the potential to influence organiza-
tional outcomes, and earlier studies provided some empirical support for this relationship, particularly with regard to board member occupation and gender.

**Occupational characteristics**

Occupational distinctions were first noted by Zald (1967) who surveyed 34 YMCA organizations and found that the proportion of business leaders on the board was associated with greater organizational efficiency and program quality, while those members with non-business backgrounds tended to have better board attendance but were not associated with organizational outcomes. The importance of occupation attributes was revealed by Pfeffer (1972) as well in his study of 80 corporations where firms requiring access to external capital had directors with financial institution backgrounds and those organizations under national regulation had higher proportions of attorneys as board members than those not under regulation.

Occupational distinctions were also investigated by Baysinger and Butler (1985) who compared the affiliation of individual directors in 266 U.S. corporations with the financial performance of those firms. Superior performing operations had a mixture of directors affiliated with top management, others who were independent of management but had occupational backgrounds as general officers of corporations, and a third component of directors with professional backgrounds (such as financial and legal) to provide advice or counsel to inside management. Although the precise composition mix varied from firm to firm in response to different organizational and environmental characteristics, the author concluded that the most appropriate board composition included a diversity in board member affiliation and occupation.

**Board member gender**

The findings from studies involving board member gender and superior organizational performance point towards boards with greater proportions of males. In one of the first studies dealing with this aspect of board composition, Babchuk et al. (1960) determined that men were more likely to be represented on boards of non-profit organizations that were ranked as highly vital to the community. In fact, Zald (1969) suggested that women rarely represented major bureaucratic organizations and thus would have less command of external resources. This notion appeared to find support in a more recent study of 100 Fortune 500 companies (Zahra and Stanton, 1988), where the ratio of board member minorities including women was inversely related to the organization's financial performance in terms of profitability and efficiency and also was inversely related to the organization's concern for customers and the environment (part of the study's social performance measure). In contrast to these results, Provan's (1980) survey of 46 human service agencies stands out as the one major study that found no relationship between the percentage of males on the board and organizational performance, represented by the agency's level of donations, which is an important resource for nonprofit organizations.

**Board member diversity**

Recently, discussions pertaining to diversity in board member characteristics have increased (e.g., Bere, 1991; Fryxell and Lerner, 1989; Houle, 1990; Mahoney, 1991; Widmer, 1989). According to Worthy and Neuschel (1984), individuals with business backgrounds and experience are still favored as candidates for board membership, but there is a growing desire for people who can bring new insights and perspectives to the board. As the authors point out, "The value of a board that balances a variety of skills and backgrounds is growingly apparent." (33).

In light of previous research showing board members with various occupational characteristics providing resources to the organization and in order to test the significance of having boards with wide representation of occupational types, it was hypothesized that

\[ H_1: \text{Greater diversity in board member occupations would be associated with higher levels of organization performance.} \]