Board Interlocking and IT Governance: Proposed Conceptual Model

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Abstract. This paper seeks to present a new dimension to the dimensions of IT governance; it proposes a model for the board interlocking and the IT governance. This conceptual model is based primarily on the Resource Dependence theory and tries to interpret the relationship between the board interlocking and the IT governance. This paper has theoretically reviewed the existing literature of the board interlocking; it has also added to the real gap in the literature of corporate governance which has not explained the importance of the board interlocking with IT governance. The researchers hope to provides a solid foundation for IT governance in order to supply companies with information about the IT environment surrounding it, the operating procedures, and the effective monitoring of the information systems, the challenges they face, the opportunities they may have, and to provide members of the board of directors with neutral opinion about these opportunities and challenges. The paper presents several contributions at both theoretical and practical levels; it paves the way for researchers to discuss the board interlocking with IT governance which contributes to the development of the theories governing the work of these concepts. It also draws the attention of the companies' administration to one of the most important practices in forming and structuring the board, i.e. the necessity of connecting the board of directors with managers who are qualified with practical experience in information systems.

Keywords: Board interlocking · IT governance · Board of director's Board independence

1 Introduction

Board interlocking is defined as the case in which directors are also members of board of directors in other Firms (Al- Mussali and Ismail 2012). Board interlocking is considered one of the commonest management practices because it is a reliable and inexpensive tool of communication that makes use of experiences (Hannschild 1993). In general, the work of members of board of directors in other corporations provides them with more

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experience in management, specifically in issues related to strategic planning (Riberio and Colauto 2016). The literature (Dooley 1969; Allen 1974; Fich and White 2005) viewed this practice from the perspective of firm's endeavors to attract experiences by employing members of board of directors of other firms, or the reason might be the absence of distinguished directors. Thus, companies try to attract them to their boards (Santos and Silveira 2007). Board interlocking is also regarded a way by which it can have an access to sources of knowledge, ideas, and capitals of other firms (Hermalin and Weisbach 2003; Weisbach 2003). Board interlocking is also considered a communication channel of knowledge transfer among firms (Shropshire 2010). Riberio and Colauto (2016) outline that in: getting external material, getting foreign support, giving a legislative status to the organization, and creating significant communication channels among organizations. Some of the other benefits of board interlocking is the ability of firms to get to the best trade partners, in addition to having an access to the strategies of certain competitive firms (Gales and Kesner 1994). There are two trends in literature: the first led by Mol (2001) assures that board interlocking enriches firms with adequate experiences and provides it with a competitive advantage through firm's information on sources of competitive companies, its creditors creativity, and development plans. Even if all this was not used to achieve the competitive advantage, it would be inevitably used to develop firm techniques and organizational environment. The second trend led by (Fich and Shivadasani 2006) sees that board interlocking has a negative impact on the market value of the company and its performance, due to the deterioration of corporate governance associated with this interlocking.

Explaining board of director's behavior depends on two main theories which are: Agency Theory and Resource Dependence Theory. Agency theory explains the role of board of directors in controlling and monitoring corporate decisions in order to mitigate agency conflicts among stakeholders of a firm (Fama and Jensen 1983). While, Resource Dependence theory explains how board of directors serves as a resource for the firm in order to reach external resources as well (Ribeiro and Colauto 2016). The majority of the literature relies on agency theory to understand board of directors, however researchers such as Eisenhardt (1990) argues that agency theory is unable to provide sufficient practical explanation due to the environmental complexities faced by board of directors in a specific environment. Due to such inability, resource dependence theory sheds the light on the importance of board of directors in reducing uncertainties found in the environment.

2 Literature Review and Developing Conceptual Model

2.1 Board Interlocking

From resource dependence perspective, firms tend to hire board directors to serve as human capital that provides the firm with effective relations that develop the firm (Hermalin and Weisbach 2003). It is also considered to be a technique to manage external resources, reducing uncertainties surrounding the firm, reducing transaction costs and linking the firm to its external environment. (Pfeffer and Salancik 1978; Williamson 1984). Board members use their reputation and personal relations to bring necessary external resources to the firm where they serve as a board director in. Despite the power and resources found in any firm, it will always need a third party that mitigates the access to external resources. That's why many firms tend to hire board members who serve in other boards. In addition to the fact that, firms need to work together to be able to protect their shared interests (Zald 1969). Corporations will always look for board members who serve their interests in other organizations, in order to increase their capital from a third party (Hermalin and Weisbach 2003) such as: the ability of the firm to gain facilitated loans with discounted interest rates due to the relations they have with financial institutions which may lead to enhance performance eventually. Davis in (Davis 1991) discovered that, during the eighties of last century, 40 American companies had board members in seven other firms at least. In Canada, it was found that between 19640–1977 there were 1600 interlocking between companies (Ornstein 1982). (Santos and Silveira 2007) tested 230 companies in Brazil between 2003–2005 and found that approximately 74% in 2003 and in 2005 69% of members had relations with other councils in Brazil. In 1997 there was 61% of interlocking among 200 big companies in Hong Kong; 69% in England and 64% in the U.S.A during the same period (Au et al. 2000). The effect of board interlocking on firm performance was handled by researchers, such as: Kim (2005) who cleared out that Korean firms has acceptable level of board interlocking which enhance firm performance, however increasing that level might harm firm performance.

Board interlocking does not only enhance firm performance, but also enhances the relation between the firm and civil society and improves firm image in the society as well. Ribeiro and Colauto (2016) mentioned that interlocking enhances the firm's relationship with societal and environmental pressure groups. Moreover, some corporations tend to hire members of such groups in the boards in order to suppress any counter act from these groups against them or getting to know their point of views early. Such action tends to improve the firms' societal image. Ribeiro and Colauto (2016) considered board interlocking as a continuous method of learning as it contributes in improving board members skills and experience and transferring knowledge in an informal way which reflects positively on their own and firm performance.

This learning, might not be always in a positive way. As some creative and unethical practices may be transferred between corporations, such as earnings management. (Chiu et al. 2013; Ribeiro and Colauto 2016) indicated that board interlocking facilitates sharing practices among corporations such as earnings smoothing. However, this might not be generalized as some studies found a positive effect for board interlocking in reducing such practices like Mindzak (2013) in his study among Canadian firms. In general, comprehending board interlocking leads to the understanding of several phenomena related to companies work. For example, Haunschild (1993) noticed that mergers and acquisitions behavior between companies is related in a way or another to board interlocking. He conducted a study on 32 firms in the U.S and noticed that processes of merging or acquisition among companies are strongly related to the relation between board of directors of such companies.

2.2 Board Interlocking and IT Governance

IT governance is defined as leadership, organizational structures, and control processes which ensure that the information technology of the company works to support and expand the company and achieve its objectives (Li et al. 2007). In addition to organizational structures that support and monitor IT operations, the company needs an external source that provides support and advice to IT operations and transactions; this source is also considered as a independent source of the company that can often have a neutral opinion. Consequently, the company's board of directors is linked to a highly experienced external source in the field of information technology. This source is fully informed about the latest developments in the world of information technology and has the knowledge and experience in order to give various opinions and attitudes to the board based on practical experience it owns in the field of information technology. Figure 1 illustrates a model for two companies; the first company is specialized in information technology development and management, and another is working in health care. The link between the boards of directors of the two companies will benefit both companies; the health care company will hire an independent board member from

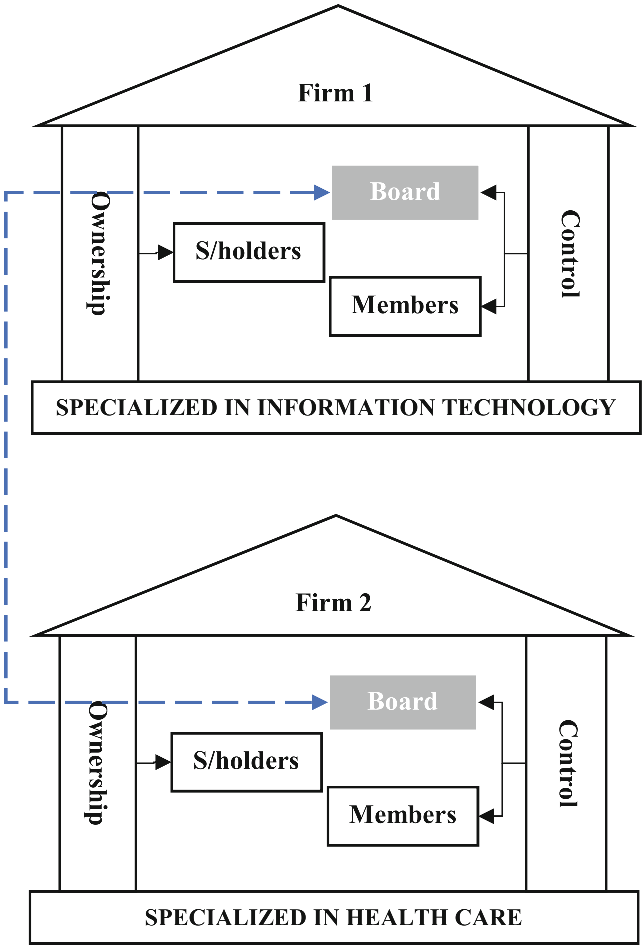

Fig. 1. Board interlocking

the other company who works in the field of information systems. This member can expert in this company and provides guidance and in the field of information systems, monitoring control, Operation procedures in addition to source of information latest be an advice and being a on the developments in the field of information systems, operations and control. For the health care company, this member will be an inexpensive source of continuing education that is supposed to provide an independent individual opinion that contribute to improving corporate governance, in general, and information systems governance, in particular. On the other hand, the company which specializes in information systems will be able to access administration files and databases of the companies that consume its products and systems in order to understand their needs and understand their decision-making powers, thus achieving a competitive edge.

The current paper investigates the relationship between board interlocking and IT governance; it is based primarily on the resource dependence theory, without dispensing the Agency theory that interprets the relationship between IT governance and the board of directors. The agency theory explains the traditional functions of the board of directors and controls the nature of its role in running the company and its operation. It includes many characteristics of the board such as the size of the board, its members' experience and the number of its meetings they hold. The resource dependence theory interprets and explains the independence of members of the board of directors as well as the interlocking between the board of directors and other boards of directors of other companies. The interlocking between the boards of directors must be deliberate and orderly, not arbitrary; the company must choose its board of directors carefully so as to provide the board of directors with the experts who are able to rationalize the decisions of the board and improve the performance of the company in general.

3 Conclusion

The interlocking among the board of directors is a common practice in companies; it works to connect the company to its external environment and provides information about the environment; it also works to identify the opportunities and risks surrounding its work. The interlocking among the board of directors is also a common practice in companies that work as suppliers and providing other companies with raw materials in addition to banks, credit and insurance institutions. However, the boards interlocking with the IT companies has not received attention despite its huge importance in providing the company with the most important developments in the world of technology, on the one hand, and providing them with specialists within its board of directors to give them neutral technical opinion on the adoption and operation of systems information as well as providing them with neutral opinions away from the administration's interests. This paper adopts a new framework for information technology governance that links the company's board of directors to the IT governance councils within the framework of the resource dependence theory through hiring independent board members who represent IT companies; the paper also invites researchers and people interested in corporate governance and IT governance to deeply research mechanisms of applying and adopting board interlocking with the IT companies, the paper of the specific factors that lead to this, in addition to the variables and the factors affecting it. Finally, interested researchers are invited to investigate the various elements that may have an impact on the performance of the company and its internal control systems and information systems.

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