

An Analysis of the Board of Directors Composition

Subjects: Others

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Practical Implications: Practical experience often supplants academic qualifications when nominating and appointing directors. Moreover, female representation on the Boards of MLCs is still lacking. Notwithstanding the fact that the importance of having separate chairperson/CEO roles is acknowledged, there is likely to be strong resistance to any law rendering this mandatory.

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Keywords: Board of Directors ; Corporate Governance ; Board Composition ; Maltese Listed Companies

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An Analysis of the Board of Directors Composition:

The Case of Maltese Listed Companies

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Keywords: *CG, Board of Directors, Board Composition, Maltese companies.*

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1. Introduction

Corporate Boards are at the pinnacle of every company and play a pivotal role in any corporate governance ('CG') system (Lipton and Lorsch, 1992), thereby making them the focal point of various efforts to improve CG (Boone *et al.*, 2006). In fact, CG codes and governance professionals have long addressed the composition of the board of directors (the 'Board'), suggesting ways in which this can be improved to allow Boards to be more effectual governance agents (Monks and Minow, 2011).

This research paper critically ascertains and analyses five aspects of board composition of Maltese Listed Companies ('MLCs'), namely board size, board independence, board expertise, gender diversity, and the chairperson/chief executive officer ('CEO') links. The study is conducted in Malta, a small island state in the European Union. It raises awareness on the need of improving CG practices relating to Board composition among Maltese listed companies. It also provides relevant suggestions assisting those in charge of CG in changing their practices and thus achieving stronger, more effective boards.

1. Literature Review

Board composition is a fundamental consideration in the corporate governance structure of a company, particularly as it influences the directors' capability of safeguarding shareholder interests. The function of the Board must therefore be underpinned by an appropriate Board composition. This study focuses on the aforementioned five aspects of Board composition within the context of the Maltese Companies Act ('CA') 1995 and the Maltese Code of Principles of Corporate Governance (the 'Code').

2.1 Board Size

The Board must be of an adequate size, such that the level of skills and experience is suitable for the entity's needs. Therefore, the optimal size of the Board shall vary on a firm-by-firm basis, depending on the firm's characteristics (MFSA, 2011). However, according to the Maltese CA1995, the number of Board members of a public company should not be less than two (Laws of Malta, 1995).

Numerous academics (Kim *et al.*, 2010; Lehn *et al.*, 2009) affirm that Boards of a smaller size function more effectually than Boards of a larger size because of the high co-ordination expenses and free-rider issues linked to larger Boards. Furthermore, with larger Boards, there is a tendency for individual directors to presume that the many other directors are monitoring. In contrast, directors in smaller Boards tend to make a greater effort than they otherwise would, since there

would be few other directors overseeing the company (Kim *et al.*, 2010). Smaller Boards also facilitate communication and decision-making among the directors and enable them to have more effectual and candid deliberations. This makes it easier to reach consensus (Lipton and Lorsch, 1992).

On the other hand, larger Boards are thought to have better and increased information and access to resources (Lehn *et al.*, 2009) as collectively Board members possess more knowledge and skills. Moreover, Boards of a larger size tend to provide better and impartial counsel to senior management. Therefore, larger Boards enhance both the monitoring and advisory role of the Board (Cohen *et al.*, 2002). Furthermore, unlike smaller Boards, larger ones are dominated less easily (Anand, 2007).

2.2 Board Independence

Directors may be classified as either executive directors ('EDs'), non-executive directors ('NEDs'), or independent non-executive directors ('INEDs') (Goergen and Renneboog, 2000). EDs are those directors who are also managers, officers or employees of the organisation (Anand, 2007). On the other hand, NEDs are directors who are not linked to the company's daily management and who are not employed by the company (Caruana, 2017). NEDs may be further categorised as independent or non-independent. Independent directors do not have any close relations with the company and are mainly inducted for their abilities and skills. Non-independent directors have a close relationship with the organisation, despite not forming part of management or being employees of the company (Anand, 2007).

The Code recommends that Boards should involve a mixture of "*executive and non-executive directors, including independent non-executives*", whose independence is to be ascertained by the Board (MFSA, 2011). However, being based on the comply-or-explain principle, the Code gives companies the flexibility not to adhere to such a recommendation.

Customarily, the concept of Board independence has been understood as a prerequisite for the Board to be able to provide effective and impartial oversight (Ringe, 2013) since INEDs are less vulnerable to capture by management (Gordon, 2006). However, the term 'independence' lacks a clear definition (Ringe, 2013). Furthermore, despite the increasing importance given to independent Board members, studies indicate a shortage of INEDs, both in Malta (Sant, 2003) and abroad (Chen and Moers, 2018). It is hard to find individuals who are completely and explicitly independent of the company's management (Kim *et al.*, 2010). Secondly, given the various responsibilities assigned to INEDs, their incentive structure is quite weak. This potentially reduces the number of individuals who are willing to fill directorship positions. Furthermore, high scrutiny from third parties, such as shareholders and regulators, has discouraged INEDs from taking on too many directorships in order to ensure that they have adequate time to dedicate to the workload arising from their existing directorships (Chen and Moers, 2018). On the other hand, others claim that the main problem is the lack of skill as opposed to the absolute independence of Board members (Davies and Hopt, 2013). Some even claim that INEDs may be too independent to comprehend the intricacies of the company which they are supposed to monitor (Nordberg, 2011). Sheer independence without knowledge regarding the entity's operations is undoubtedly improper (Gordon, 2006).

2.3 Board Expertise

The best way to manage the disruption experienced by companies today (EY, 2016) and to gain competitive advantage (Bilimoria and Wheeler, 2000) is to harness the power of different ideas from diverse groups of people (EY, 2016). To this effect, the Maltese Code recommends that the Board should ascertain that it is composed of a "*diversity of knowledge, judgment and experience*" (MFSA, 2011).

Boards can only fulfil their duties effectively and efficiently if they are properly qualified (O'Sullivan, 2009). A Board should be composed of different professional expertise to ensure that it fully comprehends all matters (European Commission, 2011). Additionally, qualified directors are also able to come up with resourceful and insightful ideas as well as to provide distinctive views (Cox and Blake, 1991). Inadequate Board qualifications lead to a lack of objectivity and critical thinking (Gaur *et al.*, 2015) (Pace *et al.* 2016).

Nevertheless, despite its importance, the CA does not specify any minimum qualifications or experience that the directors should possess (Bezzina *et al.*, 2014b)(Camilleri *et al.* 2019). Consequently, any individual may serve as a director (Mifsud, 2008). In fact, Azzopardi (2012) found that in Malta, Board members are selected on the basis of integrity and experience, rather than academic qualifications. This is troubling considering the widely recognised adversity of managing organisations and the possible consequences to creditors of an organisation incompetently managed by its directors (Muscat, 2007). However, the requirement of qualifications, whether academic or otherwise, would be impracticable to the point of being virtually impossible to implement and enforce. (Muscat, 2007) (Mazreku *et al.*2018)

Nonetheless, the Code compels Board members of MLCs to be “*fit and proper*”. This requirement is mandatory for companies operating in the financial services (Muscat, 2007). A fit and proper person shall have the personal traits, such as a good reputation (“proper”), and the professional qualifications, competence, knowledge and experience (“fit”), required for such individual to be able to adequately fulfil the duties and obligations attached to a director’s role (MFSA, 2015).

2.4 Gender Diversity

Corporate Boards are experiencing increasing pressure to appoint women. Females expand the expertise at the disposal of the management of the organisation (European Commission, 2011) since by considering females, companies are accessing wider talent pools for Board members (Adams and Ferreira, 2009). Evidence also suggests that Boards which are diversified in terms of gender carry out better oversight (Mishra and Jhunjhunwala, 2013) and are more inclined to hold CEOs responsible, thereby improving the company’s governance framework (Adams and Ferreira, 2009). Furthermore, females tend to be more autonomous (Mishra and Jhunjhunwala, 2013) since they are not part of the “old boys club” (Adams and Ferreira, 2009) and regularly attend Board meetings (Adams and Ferreira, 2009), thereby compelling enhanced attendance by males (Mishra and Jhunjhunwala, 2013).

Nonetheless, despite the extensive literature highlighting the benefits of gender diversity, the Maltese Code does not address gender diversity at Board level. This could be a major reason why Malta has the lowest presence of females in Boards when compared to other EU countries, amounting to only 5% (European Commission, 2016).

However, even globally, corporations have been slow to appreciate the capabilities of females, barring support roles (Singh, 2005), such as human resources and customer care (Higgs, 2003). This is partly because leaders tend to appoint individuals who are similar to them. As a result, Board members have become type-casted as male (Singh, 2005). Another reason which prevents women from climbing the corporate ladder is that they generally have greater childcare responsibilities, which usually results in them having less experience because of the higher tendency towards career breaks and reduced working hours. This will likewise deter women from promotions.

Other obstacles include the absence of female predecessors and role models showing that females can occupy such roles and be successful in boardrooms, and that such positions are open to women (Ford and Rohini, 2011). Comparably, the appointment of directors often relies on networks of existing directors, who are generally males. Consequently, another reason which impedes women’s presence on Boards is the difficulty experienced by potential female directors when accessing networking opportunities (Lord Davies of Abersoch, 2011).

2.5 The Chairperson/CEO links

The chairperson is responsible for the leadership of the Board (Kakabadse *et al.*, 2010), while the CEO is responsible for the leadership of the firm (Lorsch and Zelleke, 2005). Following recent corporate scandals, regulators are continuously demanding that the roles of the chairperson and CEO are held by different persons (Wilson, 2009) so as to ensure that the Board is independent from the company’s management (Lorsch and Zelleke, 2005).

In the absence of such independence, and because of the concentration of power emanating from combining the two roles, the Board will not be able to carry out its oversight and control function effectively (Duke and Kankpang, 2011). Evidently, the Maltese Code proposes that the roles of the chairperson and CEO should be separate to ensure that no one person has “*unfettered powers of discretion*” (MFSA, 2011). Yet, it permits the combination of the two roles so long as a justification is given to the market and the organisation’s stakeholders (Baldacchino, 2017).

The Code also considers the fact that in certain circumstances, combining the two roles may be inevitable (MFSA, 2011), a situation referred to as chairperson/CEO duality (Baldacchino, 2017). Proponents of chairperson/CEO duality claim that there should only be one boss (Baldacchino, 2013), otherwise the chairperson would simply be a figure-head, or else would overpower the CEO (Monks and Minow, 2011). Therefore, chairperson/CEO duality eliminates possible conflicts and power struggles between the chairperson and CEO (Solomon, 2013). Moreover, chairperson/CEO duality allows the chairperson/CEO to administer and coordinate the Board’s deliberations more competently and efficiently as s/he has a broader range of information and awareness (Solomon, 2013).

The chairperson may hold an executive or non-executive role (NACD, 2017). The Code and the King Committee on Corporate Governance (2016) recommend an independent non-executive chair since such a role reinforces Board independence, and allows a more effective assessment of the CEO (Jensen, 1993). A non-executive chair also increases the likelihood that the chair will perform his/her role effectively, and not stray away to matters concerned with the daily management of the company (Wilson, 2008). On the other hand, an executive chair may provide valuable benefits to the Board as s/he is more knowledgeable about the organisation’s limitations and opportunities and has access to critical information about the organisation’s operations and its business environment (Raheja, 2005).

The CEO may either be a Board member, a regular *ex-officio* participant, or a Board participant only upon invitation (Lieu, 2016). Those in favour of the CEO serving as a Board member assert that this provides the CEO with greater integrity and authority within the company and leads to better informed decisions since the CEO can provide inside information on the company. On the other hand, those against the CEO being a Board member argue that this is essential in keeping the management role distinct from the governance role.

However, in such cases, the CEO should still attend Board meetings (Council on Foundations, 2010). In this respect, some contend that the CEO should be normally asked to attend all Board meetings, while others argue that the chairperson should attend only upon invitation and for specific meetings, if not only upon specific matters (Lieu, 2016). In any case, it is important for conflicts of interest arising from the presence of the CEO, to be avoided, such as for instance, when the Board is setting the CEO’s remuneration, or evaluating the CEO’s performance (Council on Foundations, 2010).

1. Research Methodology

3.1 The Research Tool

The research tool deemed to be most appropriate for achieving the research objectives of this study was the scheduled semi-structured interview which was prepared after reviewing the literature summarised above to be used as a guide in order to ensure that all the questions and topics, which are required to properly address the research areas, are covered (Harrell and Bradley, 2009). The study is therefore predominantly a qualitative one where information is required directly from those experiencing the phenomenon under investigation. Since the interviews were semi-structured in nature, they provided interviewees with the opportunity to respond to the interview questions as they desired, whilst they enabled the researcher inquire further and obtain a deep understanding of the rationale of participants. Moreover, since all interviewees were probed with the same questions, the data gathered could be compared and statistically analysed (McIntosh and Morse, 2015).

The interview schedule prepared for the purpose of this study, which comprised a combination of closed-ended and open-ended questions, was aimed towards equity MLCs and Corporate Governance Experts (‘CGEs’). A five-point Likert scale, with ‘1’ being strongly disagree and ‘5’ being strongly agree, was used for the closed-ended questions.

3.2 The Sample Choice

The use of Malta as the case for this study follows the ideals of various prominent researchers such as Bezzina *et al.* (2012), Bezzina *et al.* (2014a), Briguglio, (1995), King, (1993) and Magri *et al.* (2019), who used islands and small states, as small scale laboratories for more complex politics, regulations and policies of larger countries. Moreover, this study enables us understand whether the principle of proportionality incorporated in the EU Lisbon Treaty, 2007, Article 3b, 1 and 4 work (Xuereb *et al.*, 2019).

3.3 The Sample Population

The selection of the research population is fundamental to every study (Martínez-Mesa *et al.*, 2016). Company secretaries ('COSECs') of MLCs were chosen as the target population for the study since they participate extensively in the CG function of MLCs and are fairly acquainted with the provisions of the Code. Fourteen interviews were conducted with COSECs, representing eighteen different MLCs (since two of the interviewees occupied the secretarial role for more than one MLC) out of a total of twenty four Maltese Equity-Listed Companies as at 31st March 2019. Three other interviews were also carried out with CGEs, including a representative of the Malta Financial Services Authority ('MFSA'), a corporate advisor and a corporate lawyer; their participation was deemed to be important to obtain a more comprehensive analysis of the research topic. The interviewees for this study included a combination of company secretaries, professionals working in the financial services industry and the Maltese financial regulator. The researchers have therefore sought to select the most relevant data sources to collect their research findings, and this within the context of Malta, being a small island state within a limited number of listed companies. Therefore, interviewees with past experience or who were experiencing the phenomena under study were selected with the objective of gathering the most relevant and enriching data pertinent to the research area. The interviews were deemed to be conclusive when reaching saturation (Guest *et al.*, 2006; Mason 2010; Morse 1995).

3.4 Data Analysis

Qualitative data was gathered through the open-ended questions included in the interview schedule. The researchers also probed further into the participants' rationale by asking them to elaborate further on the reasons for the responses given, thereby focusing on the participants' understanding on the subject matter under investigation. The interviews were duly transcribed and the responses were then examined using the thematic approach (Braun *et al.*, 2006) to analyse the similarities and disparities in the responses given.

3.5 Limitations and Significance of the Study

Although every effort has been made to conduct a comprehensive study on the subject matter, it remains that the study is subject to a few of limitations. Firstly, all participants in the study were Maltese and the findings of the study are therefore limited to Malta. However, this was the scope of the study so as to understand how the principle of proportionality in applying and imposing requirements works in smaller EU jurisdictions (below the 3 million population). Moreover, validity of the data as noted above was achieved at the saturation point by means of the fourteen interviews conducted with the COSECs, representing eighteen different MLCs, duly keeping in view that the interviewees comprised the most significant and relevant officers within the limited number of Maltese listed companies. Finally, in this study, emphasis was only placed on aspects of Board composition which were deemed to be more important. In particular, the element of Board diversity was restricted to gender and to the mix of qualifications and skills.

1. Findings and Discussion

An effective Board is to include an appropriate balance of a number of aspects, each of which plays its part in determining the overall suitability and relevance of such Board in governing a company. This may be closely analogous to the appropriate ingredients one is to include in a well-baked cake.

4.1 The First Ingredient: The Right Board Size

4.1.1 Small vs large boards: efficiency vs extensiveness?

The research findings indicate that the majority of respondents (11) believed that smaller Boards make it easier hold discussions. Some respondents (3) argued that it was also easier to reach a quorum with a smaller board. Yet, one participant (1) considered that such Board size is no longer considered relevant when the directors present a highly convincing argument. Moreover, it was considered by most respondents (10) that it was easier to reach consensus in smaller Boards. This is because, with fewer Board members, there is less possibility of conflict or disagreement. However, some interviewees (7) opined that the ease with which consensus is reached does not solely depend on the number of the Board members, but equally on the personalities of the directors themselves.

On the other hand, in line with the findings of Lehn *et al.* (2009) and Cohen *et al.* (2002), most interviewees⁽¹³⁾ argued that larger MLC Boards are often better able to carry out their monitoring and advisory roles, because such Boards usually have a more extensive range of skills, providing for different perspectives and superior access to resources. However, a number of respondents⁽⁶⁾ took the position that this is not always the case as the Board's ability to properly carry out its functions does not depend merely on the number of Board members, but also, and sometimes even more importantly, on the quality of the Board members themselves.

4.1.2 A perennial question: What is an appropriate board size?

The Maltese regulatory framework does not exact a maximum number to the Board of any public entity, and the only relevant proviso in the Code is that *"the Board should not be so large as to be unwieldy"*. Indeed, the majority of respondents⁽¹⁴⁾ were against the introduction of any Board capping as this would be tantamount to a rigid one-size-fits-all legal requirement for MLCs. On the other hand, without any specific legal guidance at all, difficulties will linger as to *how*, *when* and *who* is to determine such number in each MLC.

Boards may turn out to be too large or too small, unless the appropriate criteria for deciding size are taken into consideration. These criteria are to revolve around the particular circumstances of each company, and may include considerations of its industry, the spread of its shareholders, its competitors and markets, and the resulting skillsets. Company promoters and, later, those in charge of CG, need to ensure that the number of directors is and remains a fitting and balanced one even as the company progresses.

4.2 The Second Ingredient: Board independence

4.2.1 Is the Board sufficiently balanced? What are the different types of directors?

In line with the Code, Anand (2007) and Caruana (2017) contend that an ED is one who is involved in the daily operations of a company, while a NED is one who is not so involved. However, the CA (1995) does not address such difference. In fact, some respondents⁽⁶⁾ contended that the distinction between EDs and NEDs is not always a black-and-white issue. In particular, the distinction starts to become a grey area in respect of non-executive directors and the extent to which they may involve themselves in company activities without being deemed to be executive. A proper legal definition could eliminate any such ambiguity in distinguishing between EDs and NEDs, if such a definition includes some additional criteria to that of mere involvement in the day-to-day running of the organisation.

A number of respondents⁽⁶⁾ found the distinction between NEDs and INEDs to be even more vague. In this respect, Kim *et al.* (2010) argue that the determination of the independence of directors is difficult as the exact criteria have not been found. In fact, both the Code and Listing Rules merely provide a non-exhaustive list of situations which are to be considered when determining director independence. Consequently, as stated by one CGE⁽¹⁾, directors may be deemed to be independent *"even in situations when they are clearly not so"*. It may therefore be a matter of tightening up the legal framework so that it provides more clarity without becoming too prescriptive. If it is difficult to establish detailed criteria, one may rather choose to set out more examples of practical situations and case studies to help the proper ascertainment of the independence or otherwise of a Board member. For example, may additional remuneration earned in relation to the job of a director, such as that earned from being part of a Board sub-committee, be deemed to impair independence? If so, at what point may such additional remuneration become significant or material?

4.2.2 Executive, non-executive or independent directors?

In line with the Code recommendations on Board composition, almost all interviewees⁽¹⁶⁾ agreed that the Board needs to be composed of both EDs and NEDs if it is to have an adequate mix of Board members. In their view, having a balance of EDs and NEDs helps the Board to be equipped with the relevant inside and outside knowledge, objectivity and skills that are necessary to monitor, advise and formulate strategy. However, as Muscat (2007) pointed out, the Code did, and as yet does not establish any mechanism to ensure that both EDs and NEDs form part of the Board. Although the Board is responsible for the appointment of EDs, an appropriate ED/NED mix is difficult to obtain because one can hardly find executives who are both able and willing to sit on Boards. In this respect, one may argue that inviting executives as participants of Board meetings may be enough, as they will still be in a position to share their knowledge and insights with their Board. Yet, mere participation may lead to executives not being held fully responsible and accountable for their actions or for any resulting decisions made by their Board.

The Code further recommends that at least one-third of the Board is to be made up of NEDs, most of whom are to be independent. This is to help the Board ensure that its decision-making is not dominated by any member, given that, as stated by Gordon (2006), NEDs, and particularly INEDs, are less vulnerable to capture by management. However, a few of the respondents⁽⁴⁾ noted that ensuring the right balance with one-third of the members being NEDs or INEDs probably remains questionable.

4.2.3 How clear are the attributes of an independent Board member?

An INED is to have a number of attributes. All interviewees (17) maintained that the most important attribute is the ability to think autonomously from the other directors on the Board. Yet, such an attribute - symptomatic of real independence of mind - is not specifically referred to anywhere in the Maltese regulatory framework.

Another attribute found to be important by most interviewees⁽¹⁴⁾, and possibly even more relevant within this small country context, is that an INED is to have no business or family relationship with the company. While in the case of such an attribute the Code makes a specific reference, yet the definition of what a prohibited business or family relationship would actually consist of remains lacking. While previous research, such as that of Baldacchino (2017) has forwarded some examples, more research in this area would be helpful, as it is not a matter of simply emulating the position taken by other larger countries.

These clarifications may be even more enlightening if they are made in conjunction with regulatory requirements such as that of Boards having to delegate the classification of each Board member to independent consultants to determine whether they are NED or INED. Thus, this would further ensure the ascertainment of the attributes of a truly independent director without any possibility of conflict of interest.

4.2.4 Is the present twelve-year tenure period too rigid?

The majority of respondents⁽¹²⁾ agreed that, as the Code and Listing Rules stipulate, in ascertaining the independence or otherwise of a director, the tenure of a director (set at a threshold of twelve years) needs also to be taken into consideration. Yet, there are clear indications that a number of long tenures actually persist in MLCs. Could it be that the present Code recommendation of a maximum director tenure of twelve years is not always practicable? While such a fixed upper limit may normally seem to be reasonable, it is probably more acceptable for Board tenures to be set within a maximum range of five years, for instance, such as between seven and twelve years. Any tenure not adhering within such range may then be made compulsorily subject to published detailed justification. Clearly, as has already been suggested by the literature with respect to other CG measures, it is far from enough to have such maximum tenure being merely recommended by the Code. At the same time, the flexibility provided by the upper limit range helps towards ensuring that there is no shortage of members suitable to satisfy the independence criteria.

4.2.5 Is the small-country golden boy network to be tackled?

In their study, Chen and Moers (2018) found that the shortage of INEDs has been caused by the high scrutiny of shareholders which has discouraged independent directors from holding multiple directorships. In this study, most interviewees (11) instead indicated that a major factor restricting the number of INEDs is the widespread preference by shareholders and different companies for the “golden boys”, thereby resulting in the incidence of multiple directorships.

The same interviewees argued that multiple directorships may easily give rise to conflicts of interest and may discourage other persons from showing interest in directorship roles as they often perceive the situation as competing against an already established network of directors.

In this regard, a few respondents₍₃₎ asserted that the Nominations Committee ('NC') has an important role to play. In particular, it may instigate a more deeply thought-out nomination and appointment process which does not have to rely on networking. Furthermore, an internal evaluation of top management by such Committee should indicate the most capable and suitable individuals for the role of EDs. The NC, through its active processing, may also easily be in a position to recommend competent individuals for non-executive directorship roles. Unfortunately, the study indicates that as yet, most companies do not have such a Committee, as is confirmed by recent literature. This points towards the need to consider making NCs compulsory in the Maltese Listing Rules in the same manner as Audit Committees.

4.3 The Third Ingredient: Board Expertise

4.3.1 Is it formal qualifications vs experience?

Interviewees (17) were unanimous in that a mix of professional qualifications is considered crucial for Boards to fulfil their duties effectively and efficiently. This is line with the arguments put forth by O'Sullivan (2009), the EU Commission (2011), Cox and Blake (1991), and Gaur *et al.* (2015). Furthermore, having such a mix creates a competitive advantage (Bilimoria and Wheeler, 2000).

Formal qualifications and experience do not have to be alternative forms of expertise, as some respondents seem to imply. The fact that some MLCs still have a number of directors who do not hold any professional qualifications indicates that such qualifications are as yet not considered crucial in the appointment or election of directors, and this confirms the findings of Azzopardi (2012). Yet, the question arises, why, in so far as is possible, are directors not required to have both formal qualifications and experience? Probably this could be the optimal way to ensure that a Board, even a smaller one, is composed of a "*diversity of knowledge, judgment and experience*", as recommended by the Code. All interviewees₍₁₇₎ maintained that a director endowed with both qualifications and experience may be a rarity, but probably headhunting beyond "*the golden boys*" could result in unexpected gains.

Furthermore, when determining whether a director is fit and proper, the MFSA, as regulator, needs to go beyond the qualifications and experience of the individual director. It also needs to examine how far such personal attributes are compatible with those of the rest of the Board. In particular, the regulator could probably do well to pay particular attention to the overall mix of expertise where most of the directors are appointed by the major shareholders who, as also indicated earlier by Muscat (2007), tend to give too little attention to the range of expertise.

4.3.2 Is director expertise to be regulated?

Maltese law does not specify any minimum professional qualifications or experience to become a director. Nonetheless, the majority of respondents₍₁₂₎ were against any new regulatory requirements for minimum qualifications or experience. Furthermore, Muscat (2007) contended that such a requirement, particularly that relating to experience, would be both impracticable and difficult to monitor.

Being fit and proper, as required by the regulator, translates itself into being "*honest, competent and solvent*". To date, the competent authority fails to objectively define what constitutes a competent director, merely stating that this varies with the position a person holds and the "*relevant circumstances*". The question that follows concerns the manner in which the MFSA is to appropriately judge the competence of a potential candidate if there are no clearer, more objective specifications than this. As already stated, the fitness and properness of the Board as a whole also still does not seem to be given its due importance. Possibly, the MFSA might be more strongly empowered by law to compel Boards, which may be deficient as a whole in such fitness and properness, to temporarily engage a number of consultants in order to ensure that the required skill gaps are filled in.

4.4 The Fourth Ingredient: Gender Diversity

4.4.1 How relevant is gender diversity?

Despite the extensive literature highlighting the importance of having a gender diverse Board, interviewees⁽¹⁷⁾ were unanimously against any requirement with regards to the mix of female and male Board members as it is considered “*of no use, as competence is not related to gender*”. Probably, few companies realise what they have missed until they opt for such diversity.

Board competence is highly related to one's vision and experience in life. Placing together a team of men and women should result in wider perspectives and challenges with respect to various issues such as priorities in decision-making, the life/work balance, ethics and even a company's vision, mission and ultimately strategy.

4.4.2 Female board participation – to be improved?

As confirmed by the European Commission (2016), Malta has the lowest presence of female Board members. This is not a surprise given the lack of importance given to gender diversity by a few of the interviewees⁽⁴⁾ as well as the failure of the Code to address the importance of gender diversity. A number of respondents⁽⁶⁾ took the position that the weak representation of females on Boards in Malta may be probably attributed to historical and cultural reasons, which are now being increasingly challenged. Furthermore, the recent introduction of free childcare and increased emphasis on teleworking are additional motivating factors for women returners.

Yet, while such recent public measures may encourage improvement in female Board participation, this is clearly not enough. The same report (European Commission, 2016) has also remarked that Malta is one of the few countries which does not have any national measures in place to promote the presence of women on Boards. The majority of respondents⁽¹⁵⁾ were against the introduction of any gender quotas, and this is due to the fact that women may be elected to the Boards not exclusively on the basis of merit. However, it must be kept in mind, that such quotas are only a necessary evil, or rather a temporary measure to ensure that change does occur within the foreseeable future. In order not to undermine the quality and effectiveness of the Board, as claimed by many respondents⁽⁷⁾ in the study, specific measures could be taken, such as requiring formal qualifications in the case of those making use of the quota mechanism. Furthermore, quotas need to be limited to a small percentage of the Board size, say a maximum of two out of a Board of seven.

Another issue is the need for adequately changing the regulatory framework so as to encourage Boards to become much more diverse. Thus, an alternative to requiring quotas in the law is that of changing the Code itself, which by addressing such issue of gender diversity may, with its more voluntarily comply-or-explain principle, generate less resistance towards adhering to quotas.

Finally, more public investment in awareness and education on gender equality may be helpful, as it would ultimately help to change employers' and shareholders' attitudes towards more acceptance of female members on the Board.

4.5 The Final Ingredient: Dealing with Chairperson/CEO Duality

4.5.1 Are the roles of the chairperson and the CEO to be separate?

The Code proposes that the roles of the chairperson and CEO need to be separate to ensure that no one person has “*unfettered powers of discretion*” and to distinguish the Board's leadership from the management of the company. Yet, one of the provisos of the Code later allows the combination of the two roles, if an adequate justification is provided. If separating the two roles is so crucial, and given that the Code has a comply-or-explain principle, why is there a specific provision that with an adequate explanation, one may combine? Such flexibility allows power-hungry individuals to occupy both roles with little, if any, resistance. However, even with no duality of roles, the CEO may still wield significant influence on the Board, especially if s/he has been chosen by the Board itself. One reason for this is that the Board may be very much dependant on the information provided by the CEO and his/her subordinates. In fact, the matter was controversial with almost half of the respondents⁽⁷⁾ taking the position that the separation of the two roles is to be made mandatory. However, while there still exists dangers to having a separate chairperson and CEO, the problems are probably aggravated when the two roles are combined.

4.5.2 What positions are the chairperson and CEO to hold on the board?

Most interviewees (13), in line with the Code, recommended that the chairperson is to hold an independent non-executive role. As stated by Wilson (2008), a non-executive chair is more likely to focus on Board issues rather than wander onto daily management issues. Furthermore, a number of interviewees₍₅₎ argued that a non-executive chair is better able to execute the Board's control, service and strategic functions, albeit possibly suffering knowledge deficit when compared to an executive chair. On the other hand, one could argue in favour of an executive chairperson, other than the CEO, which would still be in line with the Code recommendation favouring the separation of the two roles. However, in such a case, a power struggle between the executive chair and CEO may potentially arise and be harmful to the company.

However, the Code does not make any reference to the CEO's role in the Board, particularly, whether the CEO is or is not to be a Board member. As has been indicated in the literature, a number of arguments exist both in favour and against this. This is a contentious issue. In fact, the findings indicate a general reluctance on the part of companies towards having the CEO as a Board member, with most respondents (11) contending that s/he should be an *ex-officio* participant, either on a regular basis or on call as required. This is necessary in order to ensure that Board members are provided with the necessary knowledge and expertise needed for them to take an informed decision. However, a few respondents₍₃₎ noted that if the CEO is a regular *ex-officio* participant, this may give rise to conflicts of interest, as also confirmed in the literature (Council on Foundations, 2010). Thus, they contended that it would be better if the CEO is only a participant upon invitation as this will give the chairperson the right to exclude the CEO from the meetings when potential conflicts of interest arise. Contrastingly, a number of interviewees (6) argued that the CEO is to be a Board member to place an element of onus and accountability on the CEO. Perhaps one way out of this dilemma is for the legal liability of the CEO to be specified more clearly in the regulatory framework, particularly the CA.

1. Conclusions

This study concludes that the Maltese regulatory framework, with respect to Board composition, is still lax and clearly needs to be tightened so as to spur more rigorous implementation on the part of those responsible of CG. However, there seems to be a general strong resistance to change.

While Maltese law stipulates the minimum number of directors, there is no reference to any Board size capping. Indeed, if such capping were to be strictly established by law for all MLCs, this would probably signify the imposition of a harmful and much resented one-size-fits-all approach. Flexibility is therefore needed in this connection. Too small a Board is likely to suffer from a lack of expertise, while if too large, a Board is likely to be rendered unmanageable and inefficient. The key is therefore for the company to determine its Board size in a way that ensures an adequate collective competence and willingness for the Board to be effective, and to take into account company size, scope and range of operations, along with best CG practices.

The concept of director independence seems to be quite complex and ambiguous, with much controversy as to who is and what makes a Board member truly independent. More regulatory clarity is required in this respect. While, admittedly it is much easier to be prescriptive about independence in appearance than independence of mind, yet, the CG regulatory framework probably needs to include much more emphasis on the latter. Specifically, distinctions among the different types of directors – EDs, NEDs and INEDs – need to be carefully made, clearly defining where the lines between each type are to be drawn.

With respect to Board expertise, the study concludes that, despite the fact that companies acknowledge the importance of having a Board composed of Board members holding a mix of professional qualifications, they strongly resist any legal requirements in this respect. The general view is that experience is much more valuable than qualifications, even to the extent that qualifications are too often ignored.

MLC Boards also have a low presence of female Board members, with gender diversity not being given any priority. The study concludes that the benefits of having a diverse Board are rarely appreciated, with the current impetus being that of looking narrowly at the quality of the individual Board member rather than the composite skillset of the whole Board.

A final conclusion of the study is that with regards to the chairperson/CEO links, the roles of the chairperson and CEO are separated in most MLCs. Yet, probably the best arrangements need to consist of a non-executive chairperson and a separate CEO, the latter normally participating in Board matters, but such participation is to remain subject to Board invitation.

There exists no optimal Board composition as there is no one single model of CG. Nonetheless, it is paramount to thoroughly consider the various aspects of Board composition within the context of each MLC and its operations in order to determine the composition which is best suited to each Board. Furthermore, in order to remain competitive and flourish, organisations clearly need to comprehend and appreciate the significance of enhancing their CG practices. However, for CG practices to be effective, it is not enough that MLCs subject themselves to self-regulation. There is also the need for the competent authorities to carry out the relevant statutory changes so as to improve the quality of regulation, and not just increase its quantity (Baldacchino, 2007; Baldacchino, 2017). After all, regulation is the cake recipe and, as stated by one expert in the study, *"having a good recipe goes a long way towards baking the right cake"*.

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