

The justice commissioner and the men in dark suits

Are quotas imposed by the EU the best way to increase the number of female directors, asks Stephen Levinson



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The UK is at war with Europe, again. This time it is about the compulsory presence of women on company boards. Viviane Reding, the EU justice commissioner, has threatened that if voluntary progress is not made to increase the number of women directors of publicly listed companies, she will legislate, or as she put it 'you can count on my regulatory creativity'. A robust letter from the business secretary, Vince Cable, sent on 14 September, answered this threat. It said that he had no intention of supporting such a directive and that the issue of getting more women on boards, which he agreed needed to be addressed, was subject to the principle of subsidiarity. Eight other member states also signed the letter. Shortly afterwards, Helen Grant MP, undersecretary for women and equalities, called quotas 'demeaning' and 'patronising to women'.

Ms Reding responded that this was a democratic issue and not one to be decided 'by nine men in dark suits behind closed doors'. Yet Mr Cable and his co-signatories (two of whom were in fact women) were simply indicating their (democratic) opinion that, while there were too few women on the boards of publicly listed companies, this was an issue to be resolved by member states, not centrally by EU directive.

So there is no doubt where the coalition government stands or how strongly Ms Reding feels, and battle lines have been drawn. There is opposition to the proposal from a number of EU commissioners and from Germany, although Germany was not a signatory to the letter.

As a taster of what may come, in mid-September the European

Parliament blocked the nomination of Luxembourg's Yves Mersch to the all-male European Central Bank's executive board, demanding governments come up with female candidates. The Commission had prepared a draft directive and Commissioner Reding outlined the shape of the new law in a speech on 3 October, stating that:

- she proposes to address only the share of female non-executive directors on boards, which will be required to increase to 40% 'within a reasonable time frame';
- the directive is to cover only companies listed on the stock exchange and small and medium-sized enterprises should be exempt;
- qualification is to be the decisive criterion for selection of board members and the best candidates must be chosen;
- if no equally qualified candidate from the under-represented sex is available, the possibility of a 'flexibility clause' is foreseen;
- any quota legislation should be temporary, until the objective has been achieved; and
- member states should themselves choose the sanctions for companies failing to comply with the legislation.

This framework makes clear that pragmatism and the lawyers have had some influence on Commissioner Reding. These proposals resemble s159 Equality Act 2010 in its application

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to recruitment and promotion and are, more generally, in line with Article 2(8) of the Equal Treatment Directive (76/207/EEC), as amended. The fact that the proposal is directed at non-executive directorships and is to be limited in time is presumably intended to reduce opposition. Of course, this is an early stage at which to judge how the new directive may look, as many an amendment may emerge and the proposal could be blocked entirely. On 23 October the commissioners failed to reach agreement on this proposal and were reported to have concerns about the legality of an imposed quota. The plan has to be submitted, apparently with the 40% figure as an objective rather than a mandatory quota, by mid November.

Davies report

No one disagrees there is an issue. The whole row is really about the appropriate remedy. In 2010 Lord Davies of Abersoch carried out a review in the UK, which revealed that only 12.5% of the members of corporate boards of FTSE 100 companies were women. He stated that there was a clear case for increasing that percentage, as the lack of women directors impaired corporate performance. He relied on research by McKinsey & Company, carried out in 2007, which claimed that companies with more women on their boards outperformed their rivals, with a 42% higher return on sales, 66% higher return on invested capital and 53% higher return on equity. The gloomy prediction of the Equality and Human Rights Commission two years previously had been that at the current rate of change it would take 70 years to achieve gender-balanced board rooms in the largest companies.

Despite this conclusion, Lord Davies did not recommend imposing quotas. His committee believed that board appointments should be made on the basis of business needs, skills and ability. It was plainly influenced by the outcome of the responses to its own consultation, where only 11% of respondents recommended quotas. Instead, he set a target that the FTSE 350 list of biggest companies should aim for a minimum of 25% female representation by 2015. Progress has been better than expected and in May this year the business department reported that women now accounted for one in four of all appointments or

27% of all FTSE 100 and 25% of FTSE 250 board appointments. The Government Equalities Office relies on research by the Cranfield School of Management, which indicates that by 2020 the proportion of women on FTSE 100 boards will reach 37%, almost enough to satisfy Commissioner Reding.

In keeping with the recommendations of Lord Davies, the Financial Reporting Council, with

changes attitudes. Against the use of quotas, they found that at present they are likely to lead to the promotion of less experienced executives, which may reduce performance in the short term, although more evidence is required. In addition, the imposition of mandatory rules may encourage tactics to circumvent the rules; for example there is evidence in Norway that a number of companies de-listed to achieve this.

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effect from 1 October this year, altered its Corporate Governance Code for listed companies. This now requires them to report annually on their boardroom diversity policy, including any measurable objectives they have set for themselves, and also to report on progress they have made in delivering that policy and those objectives.

Quota pros and cons

During the year the pressure to keep the issue of women on boards in the limelight has been constant. We have had the EU Commission's public consultation on gender imbalance on corporate boards, a call for evidence on the same issue from the House of Lords Select Committee on the European Union, which concluded its business on 15 October, and a Business, Innovation and Skills Committee consultation on women in the workplace, which has also only just closed.

So without challenging the desirability of increasing the number of women on corporate boards, what are the advantages and disadvantages of imposing a quota? The issue has been extensively reviewed academically. One research projects was carried out for the World Bank by Rohini Pande and Deanna Ford from Harvard. They found that there was little doubt that the imposition of a quota succeeds in increasing female leadership and that this does influence policy outcomes. There is a role-model effect that encourages other women to aspire to the highest levels of management and the presence of more women at these levels

Tackling the talent gap

Underlying all of this is the issue of an existing talent gap, which was clearly set out in the report by Lord Davies. This pointed to a marked drop in the number of female senior managers, from whose ranks directors would be appointed. The report found that the reasons for this were complicated and related to factors such as lack of access to flexible working arrangements, difficulties in achieving work-life balance and disillusionment at a lack of career progression. More simply, some women may just want to give priority to raising their children, although this was not a point made by the committee.

Given all these issues, it seems unlikely that a quota based on qualification will resolve very much in the short term. Also, if the government's expectations are correct (admittedly a leap of faith), then why bother with a mandatory approach when the UK is on course to meet targets for women on boards anyway?

It is easy to see why many have concluded that the imposition of quotas is to attack the symptoms of the problem rather than address the cause. Some add that if quotas are to be used to achieve a proportionate representation on boards on the ground of sex, why should other protected characteristics not receive the same treatment?

Whatever view is taken, the debate will intensify over the next few months. Whether it will turn into another long-running European soap opera remains to be seen but the omens are favourable. ■