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Dairy Farm Governance: Perspectives of Dairy Industry Leaders

A thesis
submitted in partial fulfilment
of the requirements for the Degree of
Master of Commerce (Agriculture)

at
Lincoln University
by
Alice Kay Sterritt

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Abstract of a thesis submitted in partial fulfilment of the requirements for the Degree of Master of Commerce (Agriculture)

Abstract

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This thesis reports on the governance requirements for New Zealand dairy farming enterprises. Over the past two decades dairy farms in New Zealand have increased in size. Owning multiple farms in a number of locations has become more common and increasingly complex business structures have developed. For many farms, succession is an issue. These developments have led to an increasing interest in governance.

This research used a case study approach to obtain the ideas and experiences of dairy industry leaders, selected based on their experience in governance. Governance literature framed the research questions and established a model that outlined the factors and roles of the board.

The interviews with the industry leaders determined that dairy farm governance is very similar to the governance principles suggested within the literature. Within the New Zealand dairy industry agency theory and stewardship theory have greater explanatory power. Therefore, ownership and operational considerations influence the board roles of strategy, control and service. Due to this influence, control is the most important of the three roles.

Factors considered important by the leaders were an understanding of the need for governance, that governance and management should be separate, the importance of outside directors, meetings should be formal with consistent agendas and adequate management reporting, directors should be selected on skill and experience and represent a wide variety of personality types. An engaged board was the preferred operational model. CEO duality, passive boards, revolving chairmen, appointing token directors, inexperienced family members or directors selected on prestige should be avoided.

Keywords: Dairy Farming, Governance, Board of Directors.
Acknowledgements

For My Grandparents

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My selected industry leaders allowed this project to take on a new dynamic for dairy farm governance research. They allowed me to delve into their personal experiences to get refreshing insights. This made for a robust and intriguing data source. This opportunity is something that I will always be grateful for. So thank you so very much to: Barbara Kuriger, Colin Armer, Jim van der Poel, Juliet Maclean, Hon John Luxton, Chris Kelly, Murray King, Sir Henry van der Heyden, Mark Townsend, David Graham and John Wilson.

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## Terms and Abbreviations

<table>
<thead>
<tr>
<th>Term</th>
<th>Abbreviation or Description</th>
</tr>
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<tbody>
<tr>
<td>Chairperson</td>
<td>Chair or Chairman</td>
</tr>
<tr>
<td>Chief Executive Officer</td>
<td>CEO or Chief Executive</td>
</tr>
<tr>
<td>New Zealand</td>
<td>NZ</td>
</tr>
<tr>
<td>United States of America</td>
<td>USA or US or States</td>
</tr>
<tr>
<td>New Zealand Dairy Board</td>
<td>NZDB</td>
</tr>
<tr>
<td>New Zealand Dairy Group</td>
<td>NZDG</td>
</tr>
<tr>
<td>Enterprise</td>
<td>Company or Business or Firm</td>
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<tr>
<td>Institute of Directors</td>
<td>IOD</td>
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Chapter 1
INTRODUCTION

1.1 Introduction to the Study

This thesis reports on the perceived need for governance within New Zealand dairy farm enterprises. Although there is a volume of research concerning corporate governance, there is very little relating to corporate governance within New Zealand dairy farm enterprises. It is surprising that more studies have not examined this, considering the economic benefit dairy farming brings to the New Zealand economy. The purpose of this thesis is to document what areas of the corporate governance literature are applicable to New Zealand dairy farms, then gain a perspective on how these relate in practice and finally test the findings against governance theories.

The need for governance within dairy farming enterprises has developed in recent years due to a change in the New Zealand industry. The main area of the New Zealand dairy industry that has changed is farm size (Kelly, 2012). Over the 30 years prior to 2010/11, the industry tripled the average herd size to 386 cows with the last 100 of these cows added in the previous eight seasons, as shown in figure 1-1 (DairyNZ & LIC, 2011). During the same period, the total effective hectares under dairying increased from under 1 million to over 1.6 million hectares, an increase of 60%.

![Figure 1-1 Dairy farm trends over a 30 year period (From, DairyNZ & LIC, 2011, p. 6)](image)

Dairy farming has become big business and the “growth of the industry means the way it is organising itself in business terms is also changing” (Institute of Directors, 2012). This growth within the industry has allowed many dairy farming enterprises to capitalise on the favourable economic climate...
to leverage their inflating equity and expand into multiple dairy farm enterprises (van Bysterveldt, 2012). The extent of this is illustrated in table 1-1 below.

**Table 1-1 Number of Farming Businesses with One or More Dairy Farms (From, van Bysterveldt, 2012, p. 19)**

<table>
<thead>
<tr>
<th>1</th>
<th>2</th>
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<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
<th>More than 11</th>
</tr>
</thead>
<tbody>
<tr>
<td>All New Zealand</td>
<td>7,586</td>
<td>1,193</td>
<td>328</td>
<td>108</td>
<td>44</td>
<td>24</td>
<td>19</td>
<td>21</td>
<td>16</td>
<td>9</td>
</tr>
</tbody>
</table>

These factors have led to an increase in the number of corporate farms and other ownership models resulting in an increased separation of ownership and control (Kelly, 2012). A potential key to successfully managing this change has been the adoption of the corporate business model, something that is currently being used with various levels of sophistication (Cooney, 2012). Millington (2012a) believes this is because top tiers of management have been slow in adjusting: “leaders of businesses that have often been built from small beginnings, sometimes do not recognise that we need to keep upgrading our skills to meet the new challenges of business management”. This statement is supported by DairyNZ spokesman Adrian van Bysterveldt, who has stated:

> “Sometimes when businesses fail it is simply because the businesses got bigger and a bit stretched in terms of their capability. They had no fall back if something went wrong. One way of protecting against that is by adopting good governance structures that lead to good decisions, review of decisions and risk management around the business. In many cases that has the effect of making the businesses more resilient” (van Bysterveldt, 2012, as cited in Tocker, 2012).

van Bysterveldt is not alone in suggesting that the dairy industry needs to move towards “adopting good governance structures”. Cooney (2012, p. 3) states that getting governance right in the dairy industry “will lift the performance of an operation to new levels”, while Kelly (2012, p. 16) suggests governance will “add significant value” to dairy farm enterprises. However, there is no elaboration by these authors on what ‘good’ governance entails. Governance and its impact on organisational performance is discussed in the literature – its definitions, theories and assumptions are known, yet to date there has been little research on how this governance applies in the context of New Zealand dairy farming.

### 1.2 Problem Statement

The objective of this research is to investigate the perceived need for governance within New Zealand dairy farming enterprises. These enterprises, by implication, are substantial businesses not only within agriculture but also within the wider business environment. Hence examination of this area regarding the success or failure of these enterprises will be increasingly important not only to the New Zealand dairy industry but also the wider economy. Therefore the problem statement that is being addressed in this research is: What are the governance needs for New Zealand dairy farming enterprises?
1.3 Motivation Behind the Research

This research is motivated by the need for foundational knowledge of the governance requirements for New Zealand dairy farming enterprises. Future performance within this industry may then be enhanced as a result of the findings and this could allow the industry to continue to excel on the world stage. This research seeks to understand current and suggested governance practices of New Zealand dairy farms through the experiences of industry leaders. From their experiences, others will be able to gain an understanding of the composition, roles, relationships and behaviours of the governing boards of New Zealand dairy farm firms.

1.4 Organisation of Thesis

This Chapter outlines why this research is important to the New Zealand dairy industry. However, before this research can be conducted, a review of the literature concerning governance is necessary. This review follows in Chapter Two.

Chapter Three, builds upon Chapter Two. This chapter identifies the gap in the literature to create central research questions. These questions help design and direct the focus of this research. The methodology used in answering these questions is then presented. This includes an introduction of the key informants for this study.

Chapter Four presents the results from the industry leaders’ interviews. This is presented in a format similar to that of Chapter Two. These results from industry leaders’ interviews are compared and contrasted with each other.

Chapter Five is the discussion for this research. This section discusses the results of the study and what they mean for the industry. This section seeks to answer the research questions. This final Chapter concludes all findings, including how this study has contributed to knowledge. Following this, are potential areas for future research. These areas build off the foundation created by this study.
Chapter 2
REVIEW OF THE LITERATURE: GOVERNANCE

2.1 Introduction
The purpose of this review is to document the literature that will help in understanding the need for governance within New Zealand dairy farming enterprises. This has been achieved by first defining governance in section 2.2. It then moves on to examine theories that have influenced governance research in section 2.3. This is followed by the roles undertaken by the board in section 2.4. The section titled ownership considerations (2.5) investigates points relating to board operation. Finally, sections 2.6 and 2.7 examine board composition and board dynamics.

2.2 Corporate Governance: Definition and Meaning
The term corporate governance is now a fashionable concept, and like many fashionable concepts, it is somewhat ambiguous and a bit of a cliché. Monks and Minow (2004) and Turner (2009) suggest that this is why we see the concept defined in a variety of different ways which are largely biased to reflect the values of those using them. Thus, one must go back to the etymology of governance to decipher what the word means. Governance comes from the Latin words guberare and gubernator, which refer to the steerer or captain of a ship. In French the word governance, spelt gouvernance, means control and the state of being governed. Thus “the etymology of the word gives us a useful metaphor, the idea of steering or captaining a ship” (Farrar, 2001, p. 3). This fits nicely with a modern definition offered by Huse (2007, p. 15) who defines corporate governance as “the interactions between various internal and external actors and board members in directing a firm for value creation”. The Cadbury Report gives a further more specific definition, which is all-encompassing as to what corporate governance is and what is involved:

“Corporate governance is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders’ role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company’s strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board’s actions are subject to laws, regulations and the shareholders in the general meeting” (Cadbury, 1992, p. 15).

This illustrates the complex nature of corporate governance, while introducing critical areas of importance within the topic that will be examined in this review.
2.3 Theories Utilised in Governance

In order to understand the context within which corporate governance research functions, it is important to examine the main contributing theories underpinning the field. This examination revealed multiple theories, with each theory primarily concerning the relationship between the shareholders, managers and the board of directors. While each individual theory was developed by examining the same relationship, all theories are different. Hence, Mowbray (2011, p. 37) suggested researchers need to take care not to utilise a “single theory in isolation as the examination of a multi-theory approach will develop greater understanding of the numerous structures and mechanisms that may enhance a board’s effectiveness”. This will help illuminate the necessary structures, mechanisms and roles that may be needed for the governance of a New Zealand dairy enterprise.

2.3.1 Agency Theory

Agency theory, which has its origins in the field of economics and finance, concentrates on two main organisational players: the agents and the principal (Fama, 1980). Specifically, agency theory “is directed at the ubiquitous agency relationship, in which one party (the principal) delegates work to another (the agent), who performs that work” (Eisenhardt, 1989a, p. 58). Thus the essence of agency theory is the separation of ownership and control (Berle & Means, 1932).

According to agency theory, within the relationship between the principal and the agent, two main problems arise. The first agency problem arises when the desired goals of the principal and the agent conflict. This suggests a rational agent and principal will choose alternative options that increase their own utility. However given that the principal relies on agents to run the organisation, the agents end up with “substantial residual control rights, and therefore discretion over how to allocate investor funds” (Clarke, 2004, p. 5). Furthermore, Eisenhardt (1989a, p. 58) suggested it is “difficult or expensive for the principal to verify what the agent is actually doing”. The second agency problem is that of risk sharing. Risk sharing arises when the principal and the agent have different attitudes towards risk, which influences their associated actions. This includes areas such as compensation, regulation, impression management, whistle-blowing, vertical integration and transfer pricing (Agrawal & Knoeber, 1996, p. 379).

One of the mechanisms to control these agency problems on behalf of the shareholders is through the board of directors (Dulewicz & Herbert, 2004; Pettigrew, 1992). Pettigrew and McNulty (1998) state that “the board will act in the best interests of the shareholder, and use their control over the decision-making process to reduce any self-interest” while Learmount (2002, p. 17) suggests this “will remove the ‘misconduct’ tendencies of management”. This is achieved by boards communicating “shareholders objectives to management and monitoring them to keep agency costs in check” (Davis, Schoorman, & Donaldson, 1997, p. 22).
2.3.2 Stewardship Theory

Stewardship theory provides a contrasting theory to agency theory (Daily, Dalton, & Cannella, 2003; Muth & Donaldson, 1998). Lane, Cannella and Lunatkin (1998) reason that agency theorists see executives as self-interested, whereas stewardship theorists observe that an executive’s own interests are often aligned with those of the owners. It is suggested that in stewardship theory:

“The model of a man is based on the steward whose behaviour is ordered such that pro-organisational, collectivistic behaviours have higher utility than individualistic, self-serving behaviours. Given a choice between self-serving behaviours and pro-organisational behaviours, a steward’s behaviour will not depart from the interests of his or her organisation” (Davis, et al., 1997, p. 23).

Davis et al. (1997) state that the behaviour of the steward is collective because the steward seeks to obtain the objectives of the organisation. This notion suggests that from the stewards perspective, the steward and the enterprise are regarded as one; where the success or failure of one is directly reflected upon the other. The stewardship principle allows an advantage as the board of directors and their CEO have a workforce which is pro-organisational in their working manner. Davis et al (1997, p. 37) suggested that stewardship theory allows the CEO and the board to be solely responsible for the “fate of the corporation, they can focus on structures that facilitate and empower rather than those that monitor and control”.

2.3.3 Stakeholder Theory

Stakeholder theory is one of the newer theories utilised in governance research, centred in ethics and social science. In the 1970s an increase in the quantity and size of enterprises and their growing role in society led to a questioning of whether corporate accountability should extend beyond shareholders alone (Tricker, 2000). Stakeholder theory suggests that enterprises have relationships or ties that impact on a wider group of people and that there is value and benefit in these relationships for the enterprise (Hill & Jones, 1992). Because of this relationship with people outside the enterprise, Hills and Jones (1992) suggest this has redefined the scope of an enterprise. This is because stakeholder theory incorporates both internal and external parties, including employees, managers, owners, customers, suppliers, competitors and the general public (Clarke, 2004; Hill & Jones, 1992). As with agency theory, stakeholder theory sees the relationship between relevant parties as a form of contract. However, there are multiple contracts which may be appropriate to the specific stakeholder (Hill & Jones, 1992). Jones and Wicks (1999) suggested that these relationships with internal and external parties impact on a wide range of components which can add fundamental value and benefit to the enterprise.

2.3.4 Resource Dependency Theory

Resource dependency theory has its origins in sociology and organisational research. Zahra and Pearce (1989) regard the board as an important resource for company performance. However, resource
dependency theorists see the board’s role is to enhance the enterprise’s prestige, reputation and legitimacy within society (Pfeffer & Salancik, 1978). Huse (2007) suggested the board of directors achieves this by providing counsel, while Mowbray (2011, p. 41) suggested this is achieved by “linking the organisation with key external resources”. Zahra and Pearce (1989) also suggest this will reduce environmental uncertainty. Thus, resource dependency theory suggests the board of directors is a channel through which additional essential resources can be obtained or acquired by their organisation (Pfeffer & Salancik, 1978).

Bryant and Davis (2012, p. 6) state that “an enterprise will act upon its environment in an attempt to reduce dependency on certain resources and to maintain independence over other resources”. This is because organisational efficiency results from an organisation’s ability to cope and minimise uncertainty, scarce resources and the substitutability of other controlled resources (Pfeffer & Salancik, 1978). Thus, the board of directors can act as a resource dependence reducing body for the organisation (Bryant & Davis, 2012).

Pfeffer and Salancik (1978, p. 248) suggest that directors can add power to an organisation when they bring the following four factors to the board: (1) Information in the form of advice and counsel, (2) Access to channels of information between the firm and environmental contingencies, (3) Preferential access to resources, and (4) Legitimacy.

### 2.3.5 Theory Summary

The examination of the above theories seeks to understand the dynamics of boards and their directors, shareholders and managers from different perspectives. Agency theory looks at the relationship between the agent and the principal and details how the separation of ownership and control can have a negative effect on the objectives of the shareholders. Stewardship theory suggests that the agent is not self-serving, as in agency theory, but has pro-organisational behaviour that leads them to act on the goals and objectives of the principal. Stakeholder theory suggests that the traditional view of a firm has adjusted and now a firm must look beyond just pleasing its shareholders and must also please other parties with which it is involved. Resource dependency theory discusses how the external resources of organisations affect the behaviour of the organisation. The interacting relationships between these variables is largely unknown in the context of a New Zealand dairy enterprise. This research will require different approaches from the single theory approach that has been the prevailing tendency in much governance research (Mowbray, 2011). By avoiding the “researchers’ tendencies to embrace a single research paradigm that fits a narrow conceptualisation” (Mowbray, 2011, p. 46) this research will be open to all possibilities, without excluding alternative explanations for effective dairy enterprise governance.
2.4 Roles of Boards and their Directors

It is commonly understood that boards are an integral part of governance (Huse, 2007; Leblanc & Gillies, 2005; Nadler, 2004). Boards are comprised of a group of individuals. These individuals are usually elected “on behalf of other people to exercise authority over an enterprise and are therefore accountable for that enterprise” (Carver, 2012, p. 149). It has been said that boards are a product of regulation (Hermalin & Weisbach, 2003, p. 9). The New Zealand Companies Act 1993 states that a company must have at least one director on the board, yet their functions are not defined (Parliamentary Council Office, 2012). Stiles and Taylor (2006) believe this leaves the board with a large degree of discretion as to what duties it undertakes. Ingley and van der Walt (2005, p. 650) state that individuals who agree to “act as board members are agreeing implicitly to meet the customary as well as the regulatory duties of directors. Therefore, they need to ask if they will influence outcomes to deliver on their duties. If they do not, the question must be raised as to why they are agreeing to accept such duties and obligations”. These duties and obligations become the underlying functions (Huse, 1990) of the board. Old (2009) suggests these underlying functions, or roles, can be categorised under the headings of strategy, control and service.

2.4.1 Strategy

The strategic role undertaken by the board is fundamental to the direction that an enterprise pursues. Huse (2007, p. 239) believes “strategy may be defined as the development, maintenance and monitoring of a firm’s core competencies with the purpose of achieving long term results and survival”.

Eisenhardt (1999) states all boards should define their split strategy focus. Huse (2007) agrees, and offers the idea of a split corporate strategy and business strategy. While corporate strategy is about defining the “type of business a firm should be involved in”, business strategy sets the standard for “how the firm should compete and position itself in relation to its competitors and business providers” (Huse, 2007, p. 239). To develop a superior business and corporate strategy, a board must have the ability to direct executive attention towards strategic decision-making as this is the cornerstone of effective strategy (Huse, 2007). According to Stiles and Taylor (2006), the collaborated work of various authors creates three different levels for a board’s involvement in strategy:

“**Legalistic:** this view stresses that the board’s role is to represent the shareholders and protect their interests. This view tends to minimise the board’s involvement in strategy and asserts that strategy development is seen as the exclusive domain of the CEO. Directors will, at the very least, monitor strategic decisions and outcomes in order to ensure they are in the best interests of shareholders

**Review and Analysis:** this perspective suggests that boards should not play an active role in formulating and implementing strategies but their role should be restricted to the review and analysis of management proposals. This echoes Fama and Jensen’s (1983) distinction between decision-management and decision-control, with management responsible for the former and the board of directors for the latter.
Partnership: this view proposes a real partnership between the Chief Executive and the board in both developing and choosing strategies for the company. Here, directors may initiate and develop strategic changes without inviting themselves to approving managerial choices” (Stiles & Taylor, 2006, p. 6).

Eisehhardt suggests that to achieve effective strategy building a firm must master four key areas:

“Set the stage: by building collective intuition through frequent meetings and real time metrics that enhance a board’s ability to see threats and opportunities sooner and more accurately.

Stimulate: quick conflict by assembling diverse teams, challenging them through frame-breaking heuristics, and stressing multiple alternatives in order to improve the quality of decision-making.

Discipline: the timing of strategic decision-making through time pacing, prototyping, and consensus with qualifications to sustain the momentum of strategic choice.

Defuse: defuse politics by emphasising common goals and clear turf, and having fun. These tactics keep the board from slipping into destructive interpersonal conflict and time wasting politics” (Eisenhardt, 1999, p. 72).

Jensen (1992, p. 4) suggests strategy is the “balancing of the present and the future, of resources, and of opportunities or threats. It is a sensitive process for the board, albeit an important one”. Williamson (2000) concludes that process will dictate the actions of the enterprise.

2.4.2 Control

Control can be seen as a question: “who has basic control over key decisions?” (Huse, 2007, p. 247). Old (2009, p. 251) expands on this suggesting control is a complex role which involves “the many aspects of being in charge of decisions and activities at any point in the year, to initiate or veto actions and to have general oversight in multiple ways”. Agency theory explains aspects of this role which defines management as an agent of the shareholders. As external actors, the shareholders are unable to engage in management (Jensen & Meckling, 1976). As such, the board must exercise control to protect shareholders’ interests due to the separation of ownership and control (Berle & Means, 1932).

The control area of governance addresses “agency arrangements and the problems that may arise when owners delegate to managers within organisations” (Gstraunthaler, Lukács, & Steller, 2007, p. 38). Under agency theory perceptions, capital should be used according to the wishes of the shareholders. To achieve this, opportunistic behaviour by management must be curbed. With their privileged access to information, management may act on their own behalf and neglect the needs of the shareholders (Ang, Cole, & Lin, 2000). Huse (2007) states boards need access to various kinds of tools and information to ensure they can implement effective monitoring and control over management. These include:
“Comparing sales, costs, balance sheet and cash flow information with earlier periods.

Information on the firms share of the market.

The minutes of management committee meetings.

Key media articles on the company and major competitors.

Consumer preference surveys.

Employee attitude surveys” (Huse, 2007, p. 248).

Stiles and Taylor (2001) suggest this needs to be expanded further. They suggest that there needs to be control at both the operational and strategic levels. They emphasise the use of an audit committee, the assessment of senior management, the role of the remuneration committee and discipline/rewarding senior management. Once these factors are considered, the board can have better control of the business for shareholders.

2.4.3 Service

The service role undertaken by the board of directors refers to the task of servicing internal actors. These service tasks are sometimes called the institutional tasks of the board as they function at the institutional level of the firm (Judge & Zeithaml, 1992). According to Old (2009, p. 28), these tasks involve “providing the organisation, particularly top management with advice, counsel and knowledge, and legitimacy and prestige, as well as access to resources by utilising networks of contacts to assist the firm”. These tasks can be further refined to represent either an internal task or an external task. Internal tasks refer to the board providing counsel to the CEO. The board members “serve as sources of information, like tentacles in the environment… where they act as generalists who can advise the CEO on all kinds of areas” (Huse, 2007, pp. 257-259). Whereas, the external service task of the board is associated with the firm’s reputation (Stiles & Taylor, 2001). It is suggested that:

“Board members with high integrity, power or reputation may make the environment positive for the firm, but legitimacy and reputation building may be more related to who the board members are than what they do. Making the board members visible may therefore be important for developing board effectiveness” (Huse, 2007, p. 257).

2.4.4 Summary of the Role of boards

The three underlying functions, or roles, of the board of directors in governing an enterprise are: strategy, control and service. The strategy role refers to setting the direction the enterprise pursues. The control role refers to the board maintaining control in order to prevent others thwarting the shareholders’ objectives. The service role refers to the board of directors providing support to the CEO or maintaining the firm’s reputation. While literature suggests that directors naturally assume these roles, corporate failures of the last decade have drawn attention to board performance, which leads many to believe these roles are not adequately undertaken. For this reason it is central to this research
to determine what part, if any, the ‘underlying functions’ play in the governance of New Zealand dairy enterprises.

2.5 Ownership Considerations

No two single enterprises are the same (Huse, 1990). This is correct with the New Zealand dairy industry. The New Zealand dairy industry is moving away from the traditional husband and wife partnership into various forms of more complex business structures. These structures include “salaried manager, variable order sharemilker, herd-owning sharemilker, salaried equity manager, equity manager on variable order, equity manager as herd-owning sharemilker, syndicates, trusts, family partnerships, family companies and government owned enterprises” (van Bysterveldt, 2012, pp. 20-21). All of these structures create a separation between ownership and control. Huse (1990) suggests that the ownership structure of a firm may be of critical importance to how a board of directors operates. Thus the board’s role in the main types of enterprises that are prevalent in New Zealand dairy farming must be examined.

2.5.1 Separation of Ownership and Control

From the discussion above it is clear that no governance model will fit all situations relevant to this research. However as identified, the issue of ownership and control will always be relevant to dairying enterprises.

The issue of separation of ownership and control has a historical basis as observations were first recorded by Adam Smith in 1776 and later by Berle and Means in 1932. Berle and Means (1932) suggested that the issue could signify a serious impairment of the social function of private property. This is explained when:

“The property owner who invests in a modern corporation so far surrenders his wealth to those in control of the corporation that he has exchanged the position of independent owner for one in which he may become merely a recipient of the wages of capital... [Such owners] have surrendered the right that the corporation should be operated in their sole interest” (Berle & Means, 1932, p. 355).

Due to the loss of control over one’s resources, a typical shareholder can no longer exercise real power to oversee managerial performance. Demsetz (1983, p. 375) suggested this allows “management to exercise more freedom in the use of the firms resources than it would if the firm were managed by its owner(s), or at least if ownership interests were more concentrated”. It is likely that this will lead to a conflict of interest as management and ownership interests will not naturally coincide. Berle and Means (1932) proposed that this conflict of interest will be resolved in management’s favour due to ownership being dispersed. Therefore this alludes to why an enterprise needs a board of directors who act as the “instrument” (Huse, 1990, p. 363), to oversee the operation to ensure it remains aligned with the interests of the owners.
2.5.2 The Role of Boards in Small to Medium Enterprises (SME)

Some researchers consider the size of the firm or enterprise to be the contextual factor that has the greatest impact on boards and governance (Huse, 2007, p. 109). Dairy farms are generally considered to be smaller businesses that fit into the SME category. Therefore, it is important to understand the characteristics that differentiate these enterprises from their larger counterparts. “Although definitions of SMEs differ in different economies, it is recognised that in all economies they are the key source of innovation, of economic renewal, of sustainable economic growth and hence, economic development” (New Zealand Small Medium Research Centre [NZSMRC], 2011). It suggested that:

“New Zealand is a nation of small business and has over 46,000 SMEs. We have adopted a definition of SMEs that encompass micro-enterprise which have fewer than 5 staff, small enterprises which have between 6-49 staff and medium enterprises which have between 50-99 staff” (NZSMERC, 2011).

In many smaller businesses, managers will predominately have the majority ownership share within the enterprise (Huse, 1990). Lockhart (2011, p. 259) suggests that this will mean the “businesses owners hold multiple roles, such as, director, trustee, shareholder, beneficiary, general manager, and labourer. For this reason Huse (1990) states that it is rare for the board to consist of more than the minimum number of members as their role becomes ‘merely subservient’. Mace (1971, p. 87) has stated that this is because an owner who also manages will “act upon their positions of power”. Lockhart (2011, p. 259) suggests that “immediate improvements could be achieved by conducting roles in isolation of each other, one at a time”. Thus, this study seeks to understand what effect this will have over New Zealand dairy farming enterprises.

While issues faced by SMEs may be less complex compared to that of their larger counterparts, they often have less internal competency to deal with these issues. This is because their boards (or lack thereof), do not have internal sources for service, expertise and control (Huse, 1990). Mace (1948, p. 88), who researched small corporations, found that “the CEO was extremely busy and they thought they did not have sufficient time to direct their thinking and actions towards anything except apparently urgent matters”. This creates weakness within the enterprise as there is no support for management, unless something is going or gone wrong, by which time it is too late. Mace (1948, p. 92) suggests that this is where a board should help as board members are “a source that can be tapped for advice and council on any problem in the operation of the business”. Hence, certain roles performed by a board for a SME may in fact be of greater importance than to a large enterprise (Huse, 2000). This study will gain the perspective of industry leaders to understand its relevance for dairy farming enterprises.

2.5.3 The Role of Boards in Family Firms

Many small firms are family owned. This is often the case within the New Zealand dairy industry (Cooney, 2012; van Bysterveldt, 2012). Bertrand and Schoar (2006, p. 74) suggest that family firms
are commonly “characterized by a concentration of ownership, control and often key management positions among family members, even after the retirement of the firms' founders”. The concept of ‘familiness’ has been developed to try to explain the uniqueness of a family firm: it refers to a bundle of idiosyncratic internal resources that exist due to the involvement of the family in the firm (Habbershon & Williams, 1999, p. 13).

It is common that the founder of a family firm has a long-term vision to continue the firm as a family firm. However only about one-third of firms are successfully transferred into the second generation, while less than ten percent continue operation into the third generation (Birley, 1986, p. 38). Bertrand and Schoar (2006, p. 75) state that there are numerous reasons for this including; “bitter feuds among family members, lack of direction, too many chiefs and not enough indians, disappointed expectations between generations and tragic sagas of later generations being unable to manage their wealth”. The “exit or failure of a significant number of these family ventures could be avoided by implementing good functioning governance mechanisms, such as a board of directors” (Bammens, Voordeckers, & Van Gils, 2008, p. 163).

For a family firm the governance controls that are recommended by Bammens, et. al (2008) are centred around three areas: task conflict, family experience and intentional trust.

Task conflict refers to disagreements by members of the family about the content of tasks, such as defining goals and strategies (Kellermanns & Eddleston, 2004). This happens when different generations and family branches get involved and the likelihood of diverging views concerning the firm increases (Dyer, 1994). Schulze, Lubatkin, and Dino (2003) claim that passive family members often create divergence between active family members. This is because passive family members want short-term pay-outs whereas active members are more content to reinvest and develop the firm.

The second governance mechanism, family experience, refers to the “tactical organisational knowledge that families develop over time” (Bammens, et al., 2008, p. 165). This knowledge goes through spikes and troughs. Miller and Le Breton-Miller (2006) suggest that families do well at passing on this knowledge from one generation to the next, however there are sometimes gaps or difficulties in the uptake of this knowledge. This is shown in figure 2.1.
Due to the transition or generational phase, the family firm is linked to the need for board control. A board will help this transition phase by allowing new members to get up to speed without affecting the dynamics and performance of the company.

The third of the three governance mechanisms for family firms is intentional trust. Intentional trust is defined as the willingness to be vulnerable to the actions of another individual based on a perception of integrity or altruism (Bammens, et al., 2008; Mayer, Davis, & Schoorman, 1995). In the short term this is beneficial to the firm as it allows them to build strong trusting relationships. However, in the long term this trust collapses as family connections become more dispersed. The newest generation will have incentives to attach a greater weight to the welfare of their immediate family than to the welfare of their extended family (Schulze, et al., 2003). The board may help to control this by steering the firm in the best direction for all who are involved.

Prabowo and Simpson (2011, p. 127) make clear the importance of independent directors on the board in order to prevent one or small groups of family members “exercising excessive control”. Since independent directors are completely unconnected to the family they can offer unbiased advice to all generations. This study will seek to see if these elements of family governance are present within New Zealand dairy farming enterprises.

### 2.5.4 The Role the Board Plays Regarding Institutional Arrangements

The term ‘institutional arrangements’ is used quite liberally in the literature. While governance and ‘institutional arrangements’ often interrelate, there is a separation between the two (Rosairo, 2010). North (1997, p. 6) offers a starting point when suggesting “institutions are composed of formal rules (laws, constitutions, rules), informal constraints (conventions, codes of conduct, norms of behaviour) and the effectiveness of their enforcement. The enforcement is carried out by third parties (law enforcement, social ostracism), by second parties (retaliation), or by the first party (self-imposed codes
of conduct). Thus, ‘institutional arrangements’ usually refer to the rules adopted by enterprises to facilitate coordination and govern relationships between stakeholders within and outside the enterprise; with many of these institutional arrangements formally defined by the enterprise’s own constitution and by legislation that occurs through their choice of business structure. Thus fundamental institutional arrangements relating to dairy farm governance will include; voting and benefit rights and entrance and exit arrangements.

2.5.5 Summary of Ownership Considerations

This section illustrates the diverse factors which may occur across different enterprise structures. The literature suggests that boards may be more important in SMEs than their larger counterparts, as SMEs often have less internal competency to deal with arising issues (Bammens, et al., 2008, p. 167). Also, family firms add further factors that need consideration when considering governance. These factors are largely on a personal level, illustrating the importance of structure, communication and control. Understanding governance factors for SMEs and family enterprises, (the two main types of dairying enterprises), may help in understanding the current governance needs for the New Zealand dairy industry.

2.6 Board Composition

It is widely acknowledged that the sources of an enterprise’s sustained competitive advantage lie not only in access to finance or capital, but within an organisation’s board (Barney, 1991; Lundy, 1994). Therefore selection of board members is foremost to "getting the right people on the bus in the right seats" (Shanker, 2007, p. 1) which will “enhance the value of the entity” (Amoako-Adu & Smith, 1995, p. 413).

In order to achieve this, the size and composition of the board is important. The general consensus is that boards should not be excessively large (Cadbury, 1992; Gstraunthaler, Lukács, & Steller, 2007; Huse, 1990; Leia & Song, 2012). The ideal number is suggested to be around seven or eight people but it is more common to see boards of 10 to 12 people (Huse, 2007; M. C. Jensen, 1993).

2.6.1 Independent Directors

It is important to understand the role independent directors play within a board. Independent directors, are directors who have “no personal or professional relationship to the firm or firm management” (Daily, McDougall, Covin, & Dalton, 2002, p. 229). These directors should bring an independent “judgement to bear on issues of strategy, performance, resources including key appointments and standards of conduct” (Cadbury, 1992, p. 58). Brewer (2010) suggests that independent directors play an important role in developing strong internal governance mechanisms which will protect the company. To achieve this there must be independent directors of sufficient calibre and number for
their views to carry significant weight. Cadbury (1992) states that one member in every six should be an independent director.

However not all researchers agree with Cadbury (1992) on the performance of independent directors. Zahra and Pearce (1989, p. 374) state “the potential impact of outside directors yields mixed results”. Amoako-Adu and Smith (1995) state that there is no convincing evidence that outside directors enhance the value of the entity. While different authors provide contradictory evidence about the value of independent directors’ roles in different enterprises, this may or may not be the case for dairy farm governance.

2.6.2 Woman as Directors

The vast majority of boards do not have woman directors (Burke, 1997; Business NZ, Institute of Directors, & Ministry of Womans Affairs, 2009; Denz, 2009). Although women make up 46% of New Zealand’s workforce they are not proportionally represented on governing boards. Within New Zealand approximately 8.6% of directors in listed companies are woman (Denz, 2009), which is similar to comparable countries. This is shown in figure 2.2 below.

Figure 2-2 Woman on Boards (From, Business NZ, et al., 2009, p. 4)

From a career point of view this makes directorships a difficult career choice for women. Some believe this is because the “old boys’ network reigns supreme” (Denz, 2009, p. 34) while others believe it’s because women encounter the ‘glass ceiling’ (Powell, 1999). The glass ceiling is “the unseen, unbreachable barrier that keeps women from rising to the upper rungs of the corporate ladder, regardless of their qualifications or achievements” (Reich, 1995, p. 4). However the former Minister of Women’s Affairs, the Hon Pansy Wong, believes “it is important that women and men stand shoulder to shoulder in our boardrooms. Combining the different strengths of men and women will provide a strong lever for business performance and competitive advantage” (Business NZ, et al., 2009, p. 2).

Evidence suggests there is a positive correlation between women in leadership and business performance (Joy, Carter, Wagner, & Narayanan, 2007). Their study looked at the performance of companies with varying numbers of women on their boards. It found the largest gap in performance
existed between those companies with no women on the board and those with three or more (Joy, et al., 2007). Another study that tracked corporate performance found that companies with two or more women on their board were more likely to be industry leaders (The Conference Board of Canada, 2001).

It is proposed by Business NZ that this is because women bring different perspectives to the board. It is suggested that this is in the following five areas:

**“Fresh perspectives:”** Boards with a balance of men and women tend to consider a wider range of issues and options, resulting in commercial decisions that are more in touch with customer needs.

**Effective leadership:** Organisational performance relies on the use of a variety of leadership behaviours, women are more likely to apply these. Therefore, by including both men and women at board level, businesses are likely to benefit from diversity of leadership as well as experience.

**Role models:** Having women on boards does lead to more women in senior management. Women in corporate leadership provide positive role models for other women entering the workforce, giving them a goal to aspire towards. A richer mix of people at board level sends a message both to the market and to staff that the company is focused on performance and talent and is open to change and innovation.

**A competitive edge:** Whether in times of growth or contraction, there will always be a need for the best talent possible in company leadership.

**Investor confidence:** Increasingly, shareholders and rating agencies are factoring into their assessments of company performance, the number of women on boards. Women will also be increasingly important investors in the future. They are likely to prefer to invest in companies that have women in leadership positions, including women directors”. (Business NZ, et al., 2009, pp. 6-7)

The support of women in governing roles makes good business sense (Schwartz, 1992). As New Zealand dairy partnerships are largely made up of a husband and wife partnership (Cooney, 2012), determining what the attitudes and current roles are for woman within the New Zealand dairy sector in relation to governance is important.

### 2.6.3 CEO Duality

CEO duality refers to the situation where the CEO also holds a position as the chairman of the board. “Different theoretical arguments have been used either to support or to challenge CEO duality” (Elsayed, 2007, p. 1204). Drawing on agency theory, those challenging CEO duality suggest that this diminishes the managerial dominance of the board (Dalton, Daily, Ellstrand, & Johnson, 1998). It is suggested that CEO duality:

“(1) constrains board independence and reduces the possibility that the board can properly execute its oversight and governance role.
(2) signals the absence of separation of decision-management and decision-control, … the organization suffers in the competition for survival.

(3) makes it difficult for insecure directors to be honest when evaluating firm performance which, in turn leads to long-term organizational drift” (Baliga, Moyer, & Rao, 1996, p. 42).

Whereas, stewardship theory has been used as an argument to support CEO duality. In the absence of opportunism, it is argued that CEO duality gives greater unity of direction and strong command and control (Huse, 2007, p. 55). It is suggested that CEOs would support this argument because non-duality would:

“(1) dilute their power to provide effective leadership of the company by increasing the probability that actions and expectations of management and the board are at odds with each other.

(2) create the potential for rivalry between the chairperson and the CEO.

(3) create confusion as a result of the existence of two public spokespeople, the chairperson and the CEO. And,

(4) limit innovation and entrepreneurship if the CEO feels that the board will perennially second guess his or her actions. (Baliga, et al., 1996, p. 42)

However Esayed (2007, p. 1250) suggested that there is not an “optimal leadership structure as both duality and non-duality perspectives have related costs and benefits. Hence, duality will benefit some firms while non-duality is likely to be advantageous for others”. As duality is a common arrangement within the New Zealand dairy farming industry and given the ownership of some dairy farming enterprises it may be important to understand how this situation could affect a dairy farming board.

2.6.4 Summary of Board Composition

In conclusion, this section has shown that there are a number of individuals who should be included on a board. Independent directors may add value to the enterprise through their independent judgment. Women may add a different perspective to the board that has been recognised as value adding, while CEO duality may add or detract from the board performance. This information may be beneficial when looking at which individuals should be on boards of directors for New Zealand dairy farm enterprises.

2.7 Board Dynamics

The key challenge facing organisations is how they continue to deliver sustained competitive advantage in the short-term while also preparing for longer-term success (Gratton, Hope-Hailey, Stiles, & Truss, 1999). The dynamics of the board are fundamental in achieving this (Laline, 2012). Thus board dynamics must be defined. Old (2009, p. 178) suggests that board dynamics are the “actions and means of key relationship maintenance”.
Laline (2012, p. 15) suggests that board dynamics have less to do with formal structures and more to do with the quality of the directors themselves and how they interact. This complements Sonnenfeld’s (2002) idea that the key to board performance is not structural but social. The most “involved, diligent, value-added boards may or may not follow every recommendation in the good governance handbook. What distinguishes exemplary boards is that they are robust, effective social systems” (Sonnenfeld, 2002, p. 109). Nadler (2004, p. 102) supports this, adding that the key lies in “better working relationships between boards and managers, in the social dynamics of board interaction and in the competence, integrity and constructive involvement of individual directors”. Ormsby (2005, p. 153) ties this social relationship together by stating individuals don’t necessarily have to be the best of friends, as long as they are travelling in the same direction.

2.7.1 The Board as a Team

A shortcoming of the literature on corporate governance is that it neglects the human side of corporate governance (Huse, 2007). The board is rarely seen as a team, yet this is exactly what it should be. Together the team is governing the enterprise towards a common goal of greater success.

One of the main reasons the board may not function as a team is “because the board meets so infrequently” (Stiles & Taylor, 2001, p. 113). The board has psychological dependence on one another because whether they like it or not, all board members are part of a group, and thus they also depend on each another (Huse, 2007, p. 210). Therefore as a team, the board should meet as often, and for as long as it needs to be able to carry out its governing duties in full (SPARC, 2009). The less the board meets, the more difficult it is to maintain continuity of thought (Nadler, 2004). However, monthly meetings can place pressure on staff (Carver, 2012; SPARC, 2009). Although a rigid structure is not suggested (Carver, 2003), the board must have some sort of schedule (Bonazzi & Sardar, 2007). Getting this balance right is critical (Leia & Song, 2012).

A team is more than the sum of its individual members. Therefore, an understanding of individual personalities will help understand the human side of governance. Leblanc and Gillies (2005) conducted a study to determine director categorisation and the resulting effect on board efficiency. These categories are in two groups: the functional director types who add to the team or board’s effectiveness and the dysfunctional types who take away from the team or board’s effectiveness. Their categories are as follows:

**Functional Director Types:**

*Conductor Chairs:* are superior chairs that relate very well to directors and management, have a keen interest in effective governance, possess remarkable leadership skills and serve at the hub of all important board activity.
**Change Agents:** act as catalysts for bringing about fundamental change (for example by replacing the CEO, fighting a takeover, developing a new strategy). Retired CEOs of successful enterprises make excellent change agents.

**Consensus Builders:** act as conciliators, disarming and resolving conflict through their interpersonal and communication skills. Former senior politicians make excellent consensus builders.

**Counsellors:** have strong persuasive skills, highly credible with the ability to work on a one on one basis with a variety of people. They are coaches, connectors, mentors and negotiators.

**Challengers:** ask tough questions. They know when to speak, what to say and how to say it, and their questions cause management to re-think key decisions. Lawyers, accountants, consultants and academics often make effective challengers

**Dysfunctional Director Types:**

**Caretaker Chairs:** are unable to run board meetings effectively, do not manage interpersonal conflict and dissent and do not have effective working relationships with other directors, the CEO or the management team. They should be replaced if they cannot improve.

**Controllers:** dominate the board process through skill, tact, humour or anger. They are very dangerous particularly when the board contains dysfunctional director types that cannot neutralise them.

**Conformists:** are non-preforming directors who support the status quo and seldom prepare for, or take part in, any serious discussion. They are well liked due to past success or relationships, and may be former CEOs, regulators or politicians who now have limited creditability.

**Cheerleaders:** are enthusiastic amateurs who constantly praise directors and the CEO and the management team but are unprepared for meetings, unaware of strategic issues facing the company and often ask inane questions. At worst they are regarded with contempt and at best they are referred to as sleepers, or as non-performers or as being ineffective.

**Critics:** constantly criticise and complain, with an abrasive tone and ill-chosen words. They are referred to as manipulative and sneaky by fellow directors and they lack the ability for constructive dissent that is possessed by challengers or change agents” (Leblanc & Gillies, 2005).

The impact of these different types of directors will affect the functionality of the board to operate as an effective team. It is a reason that many authors suggest careful selection and election of board members (Huse, 2007; Leia & Song, 2012; Shanker, 2007; Stiles & Taylor, 2001).

### 2.7.2 Board Operating Models

Authors suggest a continuum of different board operating models in the relationships between the CEO, the board of directors and management (Brewer, et al., 2010; Leia & Song, 2012; Nadler, 2004). Nadler lists these five operating models as:
“The Passive Board.” This is the traditional model. The board’s activity and participation is minimal and at the CEO’s discretion. The board has limited accountability. Its main job is ratifying management decisions.

The Certifying Management Board. This model emphasises the credibility of the board to shareholders and the importance of outside directors. The board certifies that the business is managed properly and that the CEO meets the board’s requirements. It also oversees an orderly succession process.

The Engaged Board. In this model, the board serves as the CEO’s partner. It provides insight, advice and support on key decisions. It recognises its responsibility for overseeing the CEO and company performance. The board conducts substantive discussions of key issues and actively defines its boundaries.

The Intervening Board. This model is common in a crisis. The board becomes deeply involved in making key decisions about the company and holds frequent intense meetings.

The Operating Board. This is the deepest level of on-going board involvement. The board makes the key decisions that management then implement. This model is common in early stage start-ups where top executives may have specialised expertise but lack broad management experience” (Nadler, 2004, p. 2).

Boards will slide back and forth across this scale (Nadler, 2004, p. 3). Therefore, it is important to continually re-establish where a board sits along this continuum, as board dynamics have “been analysed as a never-ending sequence of change” (Carver, 2003, p. 2). Understanding where a board is situated along this continuum, will allow the board to implement best practice to achieve greater productivity and efficiency (Carver, 2003; SPARC, 2009).

Studying the literature regarding this area may help in understanding how dairy enterprises normally operate along this continuum and how this changes in times of crisis. In recent years there have been various events that may have pushed a board along this continuum, including the global financial crisis beginning in 2009.

2.7.3 Reporting to the Board

One of the most important relationships within a company is the relationship between management and the board. The Institute of Directors suggest that the:

“Board is in charge of the governance of a company, which seeks to ensure the smooth running of a business by making accountability and oversight the core of their workings. Governance also ensures that the business has a future-facing strategic plan. This is where management comes in. They take the strategic plan and work to implement it into the day-to-day operations of the company”. (Institute of Directors, 2013)

For successful implementation of the strategic plan, the relationship between the board and management must remain complementary rather than adversarial. If the relationship becomes adversarial, the board cannot effectively govern. This is because they are unlikely to receive the
required information from management necessary to make informed decisions. In order to receive the required information there must be a method for formal reporting between managers and the board. This method must generate timely, relevant and high quality data (Millington, 2012b). Petty (2010) says boards need to refine the amount of information they allow to "filter up" from management on business issues, as unconsolidated and lengthy data wastes time, therefore preventing directors from concentrating on what really matters.

In SME’s this can get complex. When there are only one or two directors, the same directors are probably founders and these (executive) directors also manage the day-to-day operations. In this situation it is difficult to decipher what hat to wear; their owner hat or their manager hat. The Institute of Directors (2013) suggest that “for operational aspects an executive director wears the management hat, and for board meetings an executive director will need to switch to the more strategic cap (i.e. governance)”. This is where it is an advantage to have independent directors who can help guide board discussion, and make this delineation more clear.

2.7.4 Summary of Board Dynamics

In conclusion, this section has shown that there are a number of personality types that could be included on a board. Individual personality types can lead to functional or dysfunctional directors. While some directors will add value, others may detract value. This will affect how the board operates as a team. If they cannot work effectively together their board dynamics may limit their effectiveness when governing the enterprise towards the goal. This will affect the boards information flow from management, hence affecting the operating model (as outlined in section 2.7.2). Although boards are expected to move along the continuum, movement should not happen due to poor board dynamics. If the board can implement the most efficient operating model then they may achieve greater productivity and efficiency. This information regarding board dynamics may be instrumental in achieving understanding when looking at how the interactions of individuals affect the operation of the board.

2.8 Advisory Boards

It is becoming increasingly common to see a board or firm establish an advisory board. An advisory board is a “mechanism for providing the company, outside of the formality of a directorial relationship, with access to information and advice” (Anonymous, 2012, p. 1). It is “not a board of directors, nor does it aim to play any role in management” (Cooney, 2012, p. 4). An advisory board is far less formal. It consists of two or more individuals who form a team with the objectives of helping the firm achieve growth, strategic goals, identifying and managing risks and maintaining alignment with the firm’s business plan. The advisory board does not have the power to implement any decisions; therefore they are solely a tool for advice. This works in favour of both parties, as an advisory board has no legal risk. Therefore, influential and compatible people may be more interested
in committing their expertise whilst not having to directly control the enterprise. As advisory boards are far less formal, in a dairying enterprise, Cooney (2012) has found that this has helped acceptance by owners. The rules followed by and the shape of the advisory board is determined by the farm owner and their advisors. As long as the agenda or their function has been developed so as to simply prevent a talkfest, they can be instrumental in assisting the enterprise (Cooney, 2012, p. 4).

Due to the complex nature of dairy farming, consulting external sources for superior advice may add to the enterprise. Thus it is of value to this study to understand the relationships between New Zealand dairy farming enterprises and their advisory boards.

2.9 Conclusion of the Literature Review

This review of the corporate governance literature provides several points of guidance for this study into the governance of New Zealand dairy farm enterprises. This has been achieved by reviewing literature that seeks to outline the current practices, theories and assumptions surrounding corporate governance. A graphical interpretation of these findings from the literature review has been expressed in figure 2.3, which is a model adapted from Old (2009, p. 118). This figure suggests that dairy farm governance is made up of four fundamental concepts: composition, dynamics, reporting and processes. The roles of the board are strategy, control and service. These roles are interrelated and affect all aspects of board operation. Combined, these concepts and roles lead to what might be seen as a functional board for dairy farm governance. The relevant literature has been used to sensitize the researcher to governance theories to avoid the single theory approach that dominates past research. Utilising this approach in which a wide scope of corporate governance is reviewed, should provide understanding about the current situation for New Zealand dairy farm governance.
Figure 2-3 Review of Corporate Governance and the Proposed Interrelationships.
Chapter 3
THE LITERATURE GAP, RESEARCH METHODOLOGY AND DESIGN

3.1 Introduction

This chapter presents the gap in the literature in section 3.2. From this, specific research questions have been designed and listed in section 3.3. An outline of the research methodology is presented in section 3.4. This is followed by section 3.5 which examines the applicable ontology and epistemology. Section 3.6 explains the selection of the case study method, while section 3.7 introduces the industry leaders. Section 3.8 describes the techniques used for data collection, while section 3.9 describes the thematic analysis method. Finally, this chapter is concluded in section 3.10.

3.2 The Gap in the Literature

Daily, Dalton and Cannella (2003, p. 371) indicated “the field of corporate governance is at a cross road. Our knowledge of what we know about the efficacy of corporate governance mechanisms is rivalled by what we do not know”. While we have extensive literature relating to the board, its directors and their associated dynamics, we do not know if this is applicable to New Zealand dairy farms. Mace (1971) suggests that the tendency of researchers to generalise should be avoided as it is very unlikely that the governance requirements for any industry will be the same. Thus, this study seeks to uncover the current and suggested governance practices identified by industry leaders for New Zealand dairy farms, by answering the overarching research question from Chapter 1:

What are the governance needs for New Zealand dairy farming enterprises?

3.3 Specific Research Questions

In addressing the overarching research question, this research will seek to provide an understanding of the governance issues for New Zealand dairy farms. Thus the questions that will need to be answered are:

Specific Research Questions:

1. What role should governance play within New Zealand dairy entities according to dairy industry leaders?
2. What is the underpinning role of the board for dairy farming enterprises?
3. What part does board composition play in dairy farm governance?
4. What part do board dynamics play in dairy farm governance?
5. What part does board reporting play in dairy farm governance?
6. What effect do processes have on dairy farm governance?
7. Do industry leaders consider the role of dairy farming boards to be different compared to other organisations?
8. Do boards of directors add value/create additional value for dairy farming enterprises?
3.4 Research Methodology

This research utilises a qualitative research method. The rationale for choosing this method is “based on the need to explore the experience and ideas of people intimately involved” (Pangborn, 2012, p. 6) within the governance of New Zealand dairy farms. A qualitative method will achieve this as:

“Qualitative research involves an interpretive, naturalistic approach to the world. This means that qualitative researchers study things in their natural settings, attempting to make sense of, or to interpret, phenomena in terms of the meanings people bring to them” (Denzin & Lincoln, 2000, p. 3).

The idea that people bring meaning to research is highlighted by Denzin and Lincoln (2000) and supported by other authors (Hammersley, 1992; Myers & Newman, 2006; Patton, 1990). Qualitative research is concerned with “understanding the meanings which people attach to phenomena within their social worlds” (Snape & Spencer, 2003, p. 3). This research will contribute to governance literature by providing understanding and meaning that people can then attach to the phenomena of New Zealand dairy farm governance.

3.5 Epistemology and Ontology

It is suggested that the purpose of social science research is “to understand social reality as different people see it and to demonstrate how their views shape the action which they take within that reality” (Beck, 1979, as cited in Anderson & Bennett, 2003, p. 153). For this reason understanding epistemology and ontology is important within this study as it allows the researcher to uncover how participants’ “perception of human nature impacts on the approach used to reveal social truths” (Bracken, n.d., p. 2).

Epistemology and ontology are concerned with a person’s world view. Grix (2002, p. 117) defines epistemology as a philosophical theory of knowledge, whilst ontology is defined as the framework of assumptions. In this study the researcher has adopted the perspective that:

“An industry is a social system where decisions are influenced by the perceived economic conditions of management alternatives. In agriculture these alternatives are a function of the physical environment, animal biology, industry governance, consumer markets and the processes of production, processing and marketing. Epistemology defines the relationship between the researcher and the assumed reality” (Woodford, 1997, p. 15).

As this is an interpretative study, where the views of the industry leaders will help shape what good governance is for the dairy industry, “there will be a need for constant reflecting when analysing the responses to the questions to ensure that the interpretation of the response was not overly narrow or unconsciously shaped by the researcher’s own preconceptions” (Smith, 2010, p. 41).
3.6 Case Study Method

The qualitative method chosen for this study is the case study. The need for case studies arises out of the desire to understand the complex social phenomenon surrounding the function of governance within dairy farm enterprises. Case studies seek to preserve the “wholeness and integrity in which the researcher is interested” (Silverman, 2010, p. 138). This approach is the most appropriate research method, as it allows this study to document governance from the perspective of individuals in the selected industry. According to Hammersley (1992, p. 45) this is of immense importance in order to “document the world from the point of view of the people studied… rather than presenting it from the perspective of the researcher”. It is suggested that:

“The essence of a case study, the central tendency among all types of case study, is that it tries to illuminate a decision or a set of decisions: why they were taken, how they were implemented, and with what result” (Schramm, 1971, p. 6).

This research is deliberately centred on multiple case studies as the subsequent findings aim for a strong understanding of the phenomenon at hand. Yin (2009) suggests multiple cases are essential if there is insufficient background material, as each additional case will add a higher degree of certainty to the research. For this reason twelve case studies are used. The case study participants are industry leaders who have expertise within the field of governance and dairy farming. The aim is to understand the participants’ views of factors that create an effective board, by interpreting the experiences of these industry leaders.

3.7 Selection of Industry Leaders for the Multiple Case Studies

The selection of industry leaders is fundamental to the success of this research. Bluhm, Harman, Lee and Mitchell (2011, p. 6) suggest selecting “those in an organization thought to possess greater knowledge about the phenomenon under scrutiny than others may possess”. This is relevant to this study as the selected industry leaders have expertise in both governance and dairy farming.

Eisenhardt (1989b, p. 537) suggests when considering case selection, “random sampling of cases is neither necessary, nor even preferable”, while Patton (1990, p. 181) suggests “the underlying principle that is common to all these [selection] strategies is selecting information-rich cases”. Yin (2009) states when the eligible number of candidates is larger, a two-stage screening procedure is warranted. For this research, the first stage consisted of gathering relevant material about the entire pool of potential industry leaders from archival sources. This process identified individuals from all areas of the wider dairy industry including: governors, industry managers, researchers, dairy farmers and advisors. Once obtained, relevant criteria reduced the number of candidates. In this research, industry leaders were selected purposely based on their individual merit, to allow for information-rich cases. This gave validity to the research, benefiting the wider dairy industry as it is based on the real life experiences of highly respected and informed individuals.
The industry leaders are referred to by their name rather than the anonymous method. This adds further validity and depth to the research. Therefore, it is crucial that they are not misrepresented in any way. This has been partially achieved by the use of a dictaphone in order to get accurate information throughout the interview. All individuals agreed to this approach provided due care was taken whilst transcribing the interviews. All interviewees received a copy of their transcribed interviews. This gave the industry leaders the opportunity to review their comments and make corrections, alterations or deletions. Any quotes in this thesis taken from the interviews are presented in italics, and are largely verbatim. Questions from the researcher during interviews are presented in brackets.

This thesis is exempted from the requirement to receive Human Ethics Committee approval through Clause 6.2.3(2) which states that “activities ordinarily exempted from review include research projects involving interviews with and/or observations of public figures or professional persons in the areas of their duties or competence (for example, a farm manager/owner or a forestry worker, as part of a field trip), provided that this is in accordance with the provisions of the Privacy Act.”

The selected industry leaders are:

3.7.1 Colin Armer

Colin Armer is a leading North Island based dairy farmer and, together with his wife Dale, holds extensive agricultural interests. Colin started sharemilking in 1978 when he bought his first herd of 130 cows. He followed the traditional kiwi share-milking model, which allowed him to acquire his first farm in 1982. This one farm has expanded to a point where my wife and I run and own 16 farms doing 3,500,000 kgs milk solids; Armer Farms (N.I) Ltd. Colin and Dale also have considerable interests in New Zealand’s largest privately owned dairy farming company, Dairy Holdings Ltd. This started with 8 farms in 2000 and by 2013 had 72. Colin has been involved with various governance roles including LIC, Dairy Holdings and Fonterra.

3.7.2 David Graham

David has a Bachelor of Commerce and is a Chartered Accountants qualification. Aside from previously owning his own Putararu-based accountancy practice, David and his wife Ros, reside at their 350 ha dairy farm at Waotu. They also have an interest in farms in Tokoroa and Riversdale (Ballance Agri-Nutrients, 2013). David’s clients were predominately dairy farmers. I had a real interest in dairy farming. I had experience around accountancy and with people and felt that I could probably use the skills I had, in terms of governance. David stood for election for Ballance Agri-Nutrients in 1998 and was Chairman of the Ballance Board of Directors from 2003 to 2013. David was also Chairman of the New Zealand Fertiliser Manufacturers Research Association, a member of the
3.7.3 Sir Henry van der Heyden

A graduate of Lincoln University, Sir Henry holds a Bachelor of Engineering (Agr) with Honours. Sir Henry followed his parents into farming, acquiring his first property in 1985 and expanding his investment to include farming interests in both the North and South Islands and abroad. Sir Henry has contributed to industry governance for nearly 20 years. Initially what drove Henry to get involved in governance was wanting to put something back in the industry and actually setting something up for the next generation. “This included leading New Zealand Dairy Group through the process which ultimately saw Fonterra formed in 2001 and subsequent innovations in governance such as the formation of a shareholders’ council” (Auckland Airport, 2013). Sir Henry was chairman of the Fonterra board of directors until he stepped down in 2013. Sir Henry is also a director of Independent Egg Producers, Elevation Capital, Manuka SA and Pascaro. He is a member of Rabobank’s Food Agribusiness Advisory Board of Australia, ZESPRI International and New Zealand International Business Forum. For his extensive service to agriculture, Sir Henry was awarded the New Zealand Herald Business Person of the Year in 2007, and he was honoured with a Distinguished Companion of the New Zealand Order of Merit in 2009.

3.7.4 Chris Kelly

A graduate of Massey University, Chris holds a Bachelor of Veterinary Science degree. “In his earlier career, he practised as a veterinary surgeon, lecturer and advisor, and held roles in the animal health area for Glaxo Animal Health Ltd and Pitman Moore Ltd” (previously Coopers Animal Health Ltd) (Landcorp, 2013). He previously held various positions with the New Zealand Dairy Board, including Strategic Planning Manager, General Manager for Corporate Planning and Global Head of Strategic Industry Relations. Chris has extensive experience representing farmer interests to the Livestock Improvement Corporation Ltd, Dairying Research Corporation Ltd and the Animal Health Board Members Committee” (Landcorp, 2013). Chris Kelly was appointed Chief Executive of Land Corp in March 2001, a position he held for 12 years (Landcorp, 2013).

3.7.5 Murray King

A graduate of Lincoln University, Murray holds a Diploma of Horticulture and a Bachelor of Agricultural Commerce. After a period of consulting and an overseas experience (OE) Murray returned to his roots and took over management of the family farm. Murray and his wife Sarah currently farm 1650 cows across three properties in North Canterbury and Nelson, plus associated support properties (LIC, 2013). Murray has other business interests in Canterbury and overseas in dairying and farm automation. Murray also has achieved success in multiple areas off-farm. He first became involved in governance roles, as he likes to keep improving himself when the opportunities
arise. Murray’s association with LIC includes: Shareholder Councillor 2004-2009 representing the Upper South Island Wards, Former Liaison Farmer and AB Technician, Farmer submitter to Primary Industry Select Committee on LIC’s future as a result of Dairy Industry Restructure Act (DIRA 2001) and he is currently chairman of their board (LIC, 2013). Murray’s other industry interests include Fonterra Directors Remuneration Committee and the SIDE Committee. Murray is a Nuffield Scholar, has taken part in the Kellogg Rural Leadership Programme, has a Certificate in Company Direction – Institute of Directors, is a Member of the Institute of Directors and has taken part in the Rabobank Executive Development Program for Primary Producers (LIC, 2013).

3.7.6 Barbara Kuriger

Barbara has been farming for 33 years in Taranaki with her husband Louis (DairyNZ, 2013a). They followed the traditional pathway to farm ownership via sharemilking. Barbara and Louis have won several farming competitions, including the AC Cameron Rural Excellence Award in 1999. Currently they farm in partnerships with each of their three adult children and partners, two in Taranaki and one in the Wairarapa.

Barbara has had a strong interest in the agricultural industry throughout her farming career. Originally she became involved with governance roles because she loves people, and the people side of the industry which was why she wanted to be involved. She is a member of the DairyNZ Board, the Primary ITO Board, New Zealand Young Farmers Board and the Taratahi Agricultural Training Centre Board. Barbara received an AGMARDT Scholarship to attend the inaugural FAME -Food and Agribusiness Market Experience programme. She has also been a member of the Fonterra Shareholders Council including the Governance and Ethics Committee Chair. She has chaired the Livestock Improvement National Council and the NZ Dairy Industry Awards Trust. In 2012 Barbara’s contribution to the industry lead to her being awarded the inaugural Dairy Woman of the Year by the Dairy Women's Network (DairyNZ, 2013a).

3.7.7 Hon John Luxton

John received his Agricultural Science degree and Post Graduate Diploma from Massey University. Initially he was a consultant within the industry, however he decided that he was probably better to go be a farmer rather than advising people on farming. He landed in the deep end buying his first farm with 8% equity. From there John has grown to own multiple farms of his own and in conjunction with farming corporate JD and RD Wallace. As a farmer he was an A.C. Cameron Award winner. John also has an extensive off-farm career. This began with a position as an international agricultural consultant. He is a former Minister of Agriculture, and a Cabinet Minister for nine years. “John’s current directorships include the DairyNZ chairman, Landcare Research, Tatua, Wallace Corporation and the Royal NZ Ballet Company as well as a number of other businesses in which he has an interest.
He is a trustee of the Massey University Foundation, and is Co-Chair of the Waikato River Authority” (DairyNZ, 2013b).

### 3.7.8 Juliet Maclean

After completing an agricultural degree, Juliet commenced a career within the beef sector. However as it was not providing the same opportunities as the dairy sector, she switched to dairying. Juliet and her partner began 50:50 sharemilking in the Waikato. This business grew until they were sharemilking multiple properties and purchasing land. Parallel to this, Juliet was a co-founder of Synlait. From the outset, one of Synlait’s “objectives was to process their own milk and control product from cow to customer” (Synlait Farms, 2013). Juliet joined as a full-time executive in 2006. Juliet is currently CEO of Synlait Farms Ltd. She is also is a Nuffield scholar, a Massey University graduate and a member of the New Zealand Institute of Directors.

### 3.7.9 Jim van der Poel

Jim and his wife Sue live at Ngahinapouri in the Waikato not far from where Jim originally started farming. Jim took a traditional route to farm ownership via sharemilking. In the beginning they had no equity, but always made sure they had excellent cash flows and a good operating business which allowed them to leverage their business and really grow. This growth lead to ownership of three farms in the Waikato. Jim and Sue were founding members of Spectrum Group (Fonterra, 2013a). This group had extensive dairy interests in Canterbury and the USA until June 2013. Jim has had an extensive career as a governor within the industry. Jim’s involvement includes time as chairman with Dexel during its transition into DairyNZ. Similarly, Jim was involved with the New Zealand Dairy Group as it transitioned into Fonterra. In 2002 Jim was elected to the Fonterra board. “He is Chairman of the International Farming Committee and serves on the Co-operative Relations Committee. He is also Chairman of the Spectrum Group of Companies and a trustee of the Asia NZ Foundation. Jim has won a number of industry awards including the AC Cameron Award, 2002 Nuffield Scholarship, Sharemilker of the Year and the Dairy Exporter Primary Performer Award” (Fonterra, 2013a).

### 3.7.10 Mark Townshend

Mark proclaims he was one of those lucky people that knew what I wanted to do at three or four. Upon leaving school, he did a course at Taranaki Polytechnic before beginning a farming career. Mark and his wife Dianne, have ownership interests in 10 New Zealand dairy farms. The Townshend’s also have ownership interests in Canterbury Grasslands and own other businesses in the USA, Chile and Russia (Liberty Genetics, 2013). Mark became involved in governance roles in 1998. His involvement included time with the New Zealand Dairy Group where the process ultimately saw Fonterra formed in 2001. Aside from Mark’s past Fonterra directorship, he is currently a director of Pascaro Investments, Liberty Genetics, Canterbury Grasslands Ltd and he is also a director of his personal farming interests.
3.7.11 John Wilson

A graduate of Massey University, John holds a Bachelor of Agricultural Science. After a period of overseas travel, John returned to New Zealand and undertook the traditional route to farm ownership. “John and his family currently live on their dairy farm near Te Awamutu and he jointly owns a dairy farming business based in Geraldine, South Canterbury” (Fonterra, 2013b). John became involved in governance roles because he was always interested in what was happening beyond the farm gate. My absolute passion then and it still is today is on farm productions and systems and how we ensure that we are the best farmers in the world. John “joined the Fonterra Board in 2003, having previously chaired Fonterra’s first Shareholders’ Council. John became the Chairman of Fonterra in December 2012. Previously he chaired the Board’s Capital Structure Committee, and served on the Appointments, Remuneration and Development Committee, the Milk Price Panel, the Fair Value Share Review Committee, and the Trading Among Farmers Due Diligence Committee. John is also a director of Turners & Growers Limited, and a member of the New Zealand Institute of Directors. In 2000, he was awarded a New Zealand Nuffield Farming Scholarship” (Fonterra, 2013b).

3.8 Data Collection

To determine the governance needs for New Zealand dairy farming enterprises, interviews were conducted with the industry leaders. It is suggested that:

“When talking to people who are especially knowledgeable about a particular area of research or about the context within which you are researching [you will find] they are commonly in positions of authority or power by virtue of their experience or understanding. They are not naïve subjects so will not submit tamely to a series of prepared questions. It is in this respect that the interview has to be loosely structured at best” (Gillham, 2005, p. 54).

Therefore, semi-structured interviews were the primary method for data collection. The semi-structured interview “involves prepared questioning guided by identified themes in a consistent and systematic manner interposed with probes designed to elicit more elaborate responses” (Qu & Dumay, 2011, p. 246). Often this method is the most effective and convenient means of gathering information because it has its basis in human conversation; it allows the interviewer to modify the style, pace and ordering of questions to evoke full responses from the interviewee (Kvale & Brinkmann, 2009). Importantly, semi-structured interviews enable interviewees to provide responses on their own terms and in the way that they think and use language, which “proves to be especially valuable if the researchers are to understand the way the interviewees perceive the world under study” (Qu & Dumay, 2011, p. 246).

All interviews occurred in an environment where the participant felt comfortable so as to create a non-confrontational atmosphere. It is suggested that the accuracy and validity of the data collected depends entirely upon the questions that are asked (Tolich & Davidson, 2007). Therefore all questions were prepared by following Tolich and Davidson (2007) six step guide:
1) “Start by deciding what you really want to know.
2) Liaise with an appropriate research advisory group about how to approach the target group in order to find things out.
3) Draft some questions that we think might elicit that information.
4) Put them in a meaningful format.
5) Pre-test the outcome.
6) Re-write the questions” (Tolich & Davidson, 2007, p. 128).

Patton (1990) suggests that there are six different types of questions that should be asked in a semi-structured qualitative interview, each seeking to elicit a particular type of response from the interviewee. These six different question types are grounded in the following areas: demographics, experience/behaviour, opinions/values, feelings, knowledge, and sensory. This data is useful as it will provide a basis for variable analysis and help to explain the direction an individual’s opinion took. Varying question types are used so as to not lead the interviewee into a desired answer but rather promote a genuine response (Woodford, 2012). The intention is for the questions to elicit interviewees’ accounts of all aspects of their experiences. As such, any insights gained in initial interviews informed subsequent questions, as those responses may indicate an aspect of the phenomenon that has been overlooked. King and Horrocks (2010, p. 38) suggest that informing subsequent questions will add to the research “so long as you remain aware of the way that your interviewing practice developed over the course of the project, so that you can avoid such changes distorting the analysis of the data”.

3.9 Thematic Analysis

An aspect of qualitative research is that it collects a large amount of raw data. This data needs to be analysed. This analysis process is one of the “least developed and most difficult aspects of doing case studies” (Yin, 2009, p. 127). Analysis of interviewing data proceeds in two phases:

“In the first phase, you prepare transcripts; find, refine, and elaborate concepts, themes, and events; and then code the interviews to be able to retrieve what the interviewees have said about the identified themes, concepts and events. In the second phase several paths are followed. You can compare concepts and themes across the interviews or combine separate events to formulate a description of the setting. In doing so, you seek to answer your research question in ways that allow you to draw broader theoretical conclusions (Rubin & Rubin, 2005, p. 201).

Fereday and Muir-Cochrane (2006) suggest that this needs to be further refined through a hybrid process of inductive and deductive thematic analysis to interpret raw data. Thematic analysis is a systematic “method for identifying, analysing and reporting patterns (themes) within data” (Braun & Clarke, 2006, p. 79). The main strength of thematic analysis is that it enables the use of a wide range of information in a systematic manner that increases the accuracy in understanding and interpreting
This makes thematic analysis ideal for this study. The main phases and processes of thematic analysis, as suggested by Braun and Clarke (2006) are:

**Table 3-1 Phases of Thematic Analysis (From, Braun & Clarke, 2006, p. 87)**

<table>
<thead>
<tr>
<th>Phase</th>
<th>Description of the process</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Familiarizing yourself with your data:</td>
<td>Transcribing data (if necessary), reading and re-reading the data, noting down initial ideas.</td>
</tr>
<tr>
<td>2 Generating initial codes:</td>
<td>Coding interesting features of the data in a systematic fashion across the entire data set, collating data relevant to each code.</td>
</tr>
<tr>
<td>3 Searching for themes:</td>
<td>Collating codes into potential themes, gathering all data relevant to each potential theme.</td>
</tr>
<tr>
<td>4 Reviewing themes:</td>
<td>Checking if the themes work in relation to the coded extracts (Level 1) and the entire data set (Level 2), generating a thematic ‘map’ of the analysis.</td>
</tr>
<tr>
<td>5 Defining and naming themes:</td>
<td>On-going analysis to refine the specifics of each theme, and the overall story the analysis tells, generating clear definitions and names for each theme.</td>
</tr>
<tr>
<td>6 Producing the report:</td>
<td>The final opportunity for analysis. Selection of vivid, compelling extract examples, final analysis of selected extracts, relating back of the analysis to the research question and literature, producing a scholarly report of the analysis.</td>
</tr>
</tbody>
</table>

This research demands a detailed coding process due to the depth of data. Crabtree and Miller (1999) recommend developing a code manual as it serves as a data management tool for organising segments of similar or related text to assist in interpretation. This code manual is to be held loosely so as not to test theory and impose a specification of constraints on the data (Eisenhardt, 1989b). A template was developed based around the research questions. Once this template was developed, it was tested. This tested the applicability of the code to the raw information (Fereday & Muir-Cochrane, 2006). At this stage transcripts were entered as documents into the NVivo computerised data management programme. This software allows for qualitative inquiry beyond coding, sorting and retrieval of data. The complete six step process helped the overarching or core themes that were identified, and captured the phenomenon of governance requirements for large dairy farms.

**3.10 Conclusion**

This chapter has outlined the specific research questions and the research methodology and design used in this study. The qualitative research approach utilised semi-structured interviews. Through the use of case studies the selected industry leaders were able to comfortably express their knowledge and experience concerning the governance of New Zealand dairy farms. Thematic analysis was the technique used to analyse the data gathered from these interviews as it presents the most suitable technique for drawing conclusive findings. The next chapter presents the results of the interviews.
Chapter 4
RESULTS

4.1 Introduction

The previous chapter described the benefits of the qualitative research approach, the rationale for its selection in this research and the process by which industry leaders were selected. The selection process was described in detail, including the criteria for selection based both within the on-farm environment and on their wider industry environment. All industry leaders were asked the same questions from the ‘interview schedule’ (see section 5.16). Using a thematic approach, the results from the interviews are discussed in the following sections. The answers to similar questions were grouped together and presented as one. The following section (4.2) state what governance means for dairy farming enterprises. Dairy farming governance and industry governance are contrasted in section 4.3. Section 4.4 discusses board composition and section 4.5 presents the findings on board meetings. This is followed by the results of a board’s involvement in strategy and vision (4.6). Section 4.7 highlights exit and entry and the shareholders agreement. Section 4.8 reflects the future challenges for the industry. Lastly, section 4.9 is on the findings on board operating models.

Data from the transcribed interviews is mainly verbatim, and printed in italics. The quotations are ascribed to each individual using the individual’s names in brackets at the completion of the quote or sometimes proceeding the quote.

4.2 The Establishment of Governance

Governance is not a new concept. However, New Zealand dairy farm enterprises have taken a gradual approach to implementing its principles. This section looked at the industry leaders’ perspectives on why dairy farming enterprises have implemented governance and with what effect. This has been broken into five sections.

4.2.1 Governance for Dairy Farming Enterprises

When reflecting on why they had or had not established a level of formal governance over their own farming interests, the industry leaders gave an array of answers. This ranged from having no governance, to full governance. The reason for this variation is due to the ownership and operational considerations surrounding the enterprise in question. In fact, many industry leaders noted that they have established different governance models over different enterprises in which they are involved. It is important to establish a level of governance that is suitable to the enterprise. For this reason they suggested that the establishment of governance is not something to be taken lightly (Colin Armer).
Those who had not established governance or who had a simplified level of governance have done so purposely. This was for two reasons; the enterprise did not require a complex structure or they did not want to reduce their control. A number of sources indicated that their personal interests, which are relatively simple in context, didn’t require a high degree of governance. An example of this would be in Jocelyn and my personal business, we are the two directors of the board. [However] we do not have board meetings. That’s probably a pretty standard [situation] in New Zealand (Henry van der Heyden). This is supported by another participant who suggested how he achieved the appropriate level of governance: We do not have a board. This is because Sue and I are sole traders. We employ managers and they report directly to us. So we direct, directly through that process (Jim van der Poel). The second identified reason for having little formal governance was because it would mean a shift in control. Murray King noted that he, like many New Zealand dairy farmers, likes to be in control. This was affirmed by David Graham: I have not implemented governance to the same degree. I am much more hands on in my approach. If David or Murray were to have a formal governance system, they would not have full control and would be held accountable for their decisions: I probably do not want to justify my actions to anybody else (Murray King).

The above quotes refer to personal farming interests; interests that are currently less complex and have a higher level of personal engagement than their associated farming interests. This may explain why they have a simplistic or no form of governance over these interests. The following quote from Chris Kelly explains at what point he believes the requirement for formal governance becomes an issue:

Think of where the farm is positioned. One extreme is a 200 cow, 50-year-old farmer in Taranaki, I do not think that he or she has a problem. They do not need much more governance than they already have. That is one extreme. If you take the next extreme which is Dairy Holdings or Landcorp who are the two biggest holders of dairy land in New Zealand, you then have to go to the full management structure and have a board, a CEO, and all the usual things. Then there is a whole range of things in-between. I think that the grey areas are the areas where farms are not big enough to be corporate but bigger than just an ordinary little family farm. So size is an issue for governance. Multiple ownership is another issue, where you have multiple owners you will have competing interests of shareholders and that is where you need a good governance structure. Another issue involves looking at things like succession planning which is quite emotional and often when families are involved, it is often better to have a good governance structure. Therefore, depending on the position of the farm and those different criteria, this will then depend on whether you will need a formal structure or just keep going the way that you have. (Chris Kelly)

In addition to those mentioned by Chris Kelly, a number of sources identified the following factors necessitating the change to a higher level of governance: scale, multiple ownership, succession, pursuit of a new direction, and location. Scale referred to the size of the business and the geographical location of the business. Multiple ownership referred to the number of individuals that collectively own a share of the enterprise. Succession referred to the process of passing the asset onto another party, while the pursuit of a new direction referred to a change in the enterprise’s strategy.
One example of a governance requirement change required by location was given by Henry van der Heyden: *Once you get complexity through the entire business, including the shareholders, you have to put in processes and a formal governance system.* This example contrasted the governance requirements of his personal business to that of Manuka (an international dairy farming company located in Chile). Jim van der Poel also notes the same change in governance requirements when referring to Spectrum (a dairy farming company located in Canterbury): *as it grew two things we needed was structure around the management and proper governance roles. It continued to evolve from there.*

### 4.2.2 Governance and Financial Value

The industry leaders were asked whether they had found a financial benefit to establishing governance over a dairy farming enterprise. The industry leaders largely said yes, but there were some provisos.

Those who stated that a governing body would add value were talking contextually, as *governance structure is important* (Murray King). As suggested by the results in section 4.2.1 there are different governance requirements for different enterprises. If the right level of governance for the enterprise in question is established, then *I think that the cost would be easily recompensed* (Murray King). Chris Kelly adds *boards have been around for centuries, and they are there for good reason.* Some of the ways that value is generated by these boards includes: *to separate governance from management, challenge management on behaviours and decision-making, big picture view, shareholders peace of mind that their investment is protected* (Chris Kelly), *it gets you out of a muddle and provides direction* (Barbara Kuriger), *risk management* (Colin Armer), *discipline and value protection* (Jim van der Poel). Henry van der Heyden gave some examples of these elements in New Zealand dairy farm businesses:

*I’ll give you some examples of how governance adds value. Most farmers have a budget. What farmers do is throw the budget in the bottom drawer. The first step for the board would be to sort a formal budget and test it. A board will hold the person running your farm or your business to account against the budget. Quite a few farming businesses do that: but how many farming businesses have a three to five year business plan? Now at the heart of corporate governance are processes, including a three to five year business plan. Once you have got those things in place I think you actually de-risk the business. Also, banking becomes easier; your banking margins are reduced. I am probably involved in three or four very highly leveraged large businesses, $200,000,000 farming businesses, and the banks get huge amounts of comfort that there is actually a governance body in place.* (Henry van der Heyden)

The example above on budgeting introduces the concept of accountability. A budget accounts for every bit of expenditure within the enterprise. By conducting a formal budget and testing it, a board are able to see if there are any financial weaknesses that can be improved. This budget can then be used as a mechanism of control to reign in any self-serving behaviour from management and keep the enterprise aligned with the shareholders’ wishes. A business plan is another useful tool. This requires
that a strategy be written, thus providing direction for the enterprise. The combination of these two processes ‘de-risks’ the business as the accountability and direction provided means the board has greater control. Henry van der Heyden mentions that this makes some relationships easier such as with banks. This is because external parties have a greater level of confidence in the business. Thus, this adds value to the enterprise.

Those who suggested that there are some provisos to a board adding value, referred to the board removing some of the enterprise’s dynamism. Without a board, the industry leaders referred to risk taking (Colin Armer) and decision making on the run (Jim van der Poel). They believe having a board from the initial stages may remove some of their ability for rapid growth. This is because if you had to go to a board of directors and spell out those risks in writing and weigh them up and you had to get approval from your board I suspect some of ours would have been turned down (Colin Armer).

### 4.2.3 Important Aspects when Establishing a Dairy Farming Board

The industry leaders were asked what they perceived to be the ‘important’ tasks and roles involved in establishing a dairy farming board. The industry leaders all had slightly different experiences when setting up a board. However many of their ‘must do’s’ centre around the composition, competencies and the selection process of directors. It was suggested that this was the most important ‘must do’ when establishing a board because you should get people who can add value to the business (John Luxton). The selection process is very important as explained in the quote below:

> You must spend a long time on deciding the makeup of your board. For example, should it be all internal, which I suggest it should not be. Should it be all external, which I also suggest it should not be. Then decide the size of the board. When recruiting directors, pretend that you are recruiting a person or employee for your company. Spend as much time as you would in that process to ensure you are selecting the right directors. Do not pick your mates for want of a better word. Treat it as if you were employing someone to work for your organisation and then put in as much time and effort as you would otherwise do. (Chris Kelly)

Other industry leaders spoke of composition but specifically the importance of establishing independent directors. This is because independence brings different insights (David Graham). Both Colin Armer and David Graham suggest independents are critical to the success of the business because their outlook or agenda is not influenced by a financial interest. For this reason, they believe the more the merrier.

Other industry leaders suggested that their ‘must do’ was for the enterprise to clearly understand why you want to have a board (Colin Armer). Juliet Maclean states the board must be set up with a clear purpose of what they want to achieve. This is explained in further detail in the below quote.

> You very clearly need to understand what governance is about and what management is about. From what I see there are a lot of boards that function very poorly because they hover somewhere in the grey space between governance and management. So understand the
outcome that you want, and make sure that the directors understand that. I think the other must do’s are to be very honest about the skill required, the fit, and sticking to your guns on making sure that that is clear. You need to be prepared to be absolutely honest with your information, timely with your information, open to the feedback and prepared to have the robust and bold conversations that are going to facilitate change. It is not just a back scratching exercise to tell you that the cows and grass look nice. (Juliet Maclean)

The preceding quote highlights the importance of selecting individuals who have the ability to govern the business rather than interfere with management. These two roles need to be kept separate so that the enterprise has accountability. Juliet Mclean suggests that if you are in doubt do not appoint a director. Reporting is also mentioned as a must do. This suggests that information needs to be relevant and timely if it is to be of any use to the board for decision-making.

4.2.4 Governance Hindsight

The industry leaders were asked to reflect on their personal experiences with dairy farm governance. In doing so, they were asked if there was anything that they would do differently. The majority of the industry leaders said there was nothing that they would now do differently. John Luxton and Jim van der Poel suggested that this may have been due to their governance knowledge which allowed them to react to the different needs as the business evolved. Juliet Maclean supported this when she talked about reflecting on the board and how the board developed to meet the enterprise’s requirements.

However, some industry leaders noted aspects that they would now do differently. Barbara Kuriger suggested she would spend more time establishing the structure of the enterprise as she believes that structures should be simpler. John Wilson suggested they got their governance system right, the only thing that we would have done differently is we would have bought more land and grown faster. Colin Armer also believes that their group should have spent more time talking about their strategy:

I think I would have been far more clear about the fact that I didn’t need any dividend, and I didn’t want any dividend, I wanted to regrow everything. Although shareholders initially agreed with this, time changed them. We should have allowed for that changing of events. (Colin Armer)

This shows the importance of talking every aspect of the business through before establishment.

4.2.5 Advisory Boards as a Governance Middle Ground

As suggested earlier in this section, there is a ‘grey area’ between the two extremes of governance (no governance to formal governance). One suggestion is the use of an advisory board to cover this ‘grey area’ and meet between the extremes as a governance middle ground. As explained in section 2.8 (p.23), an advisory board is a mechanism for providing the company, outside of the formality of a directorial relationship, with access to information and advice that is not legally binding. When the industry leaders were asked what they thought of this there was a clear division in their answers.
Several of the industry leaders noted that an advisory board does work (Chris Kelly) but it depends where you are on the governance scale (David Graham). Supporting reasons that were given included receiving input from others in a less formal manner (Barbara Kuriger). She suggested that this approach was a very good way to learn, even though it is informal, because it is always good to have other people ask questions of your business. David Graham echoed Barbara when he added you can always learn from everybody and anybody. The more you talk about things the better. Mark Townshend spoke of his experience with advisory boards when he spoke of the following benefits:

> When you are a farmer you are expected to be good at a lot of things. You are expected to be good with cows, pasture, labour, financials and repairs and maintenance. So there are five boxes there, and there are not many people who tick more than three of the five boxes. So knowing your own weaknesses becomes a strength in itself. If you are going to bring in an advisory board don’t bring in somebody who is going to tell you what a good job you are doing on the things that you are good at, because that is often the case. You have to go out and find people who are good at the things you are not good at and the boxes you cannot tick. (Mark Townshend)

Other industry leaders were against the concept of an advisory board. Terms such as weak concept (Henry van der Heyden) and waste of time (Colin Armer) were used when referring to its value. Chris Kelly explains that is because an advisory board has no teeth which allows management to ignore it. Henry van der Heyden explains this further when he speaks of the difference between a board and an advisory board:

> [With a board] the accountability and the responsibility of the business shifts from the individual family to the board. So suddenly, the whole responsibility of that business has actually shifted. With an advisory board you can give advice until the cows come home but it’s that shift that you are looking for because that’s how you de-risk the business and that’s where the value is actually created. (Henry van der Heyden)

### 4.3 Differences between Dairy Farm Governance and Industry Governance

The industry leaders were asked about the key differences between their roles as a dairy farm director and a dairy industry director. This section contrasts and compares their responses between dairy farming governance and industry governance, the benefits of having external governance experience, and how a family business affects governance. It also gives an example of how an unforeseen event impacted on governance.

#### 4.3.1 Industry Governance versus Dairy Farm Governance

The industry leaders were asked what they perceive as the key differences between their roles as a director in the governance of dairy farming interests versus their industry governance. There was little variation in the responses as every industry leader stated that the principles are the same.
The industry leaders stated that there is no difference in the way a dairy farming business should be governed when compared to the large industry organisations in which many are involved. Jim van der Poel suggests that the principles of governance are the same; it is the level of issues that you are dealing with which increase in complexity.

### 4.3.2 Utilised Knowledge

The industry leaders were asked if there is any information or knowledge that they have taken from their industry governance roles and implemented back in their personal dairy farming interests. All the industry leaders suggest that they have picked up various ideas, whether consciously or subconsciously, which allows those experiences that you have to be part of who you become (Jim van der Poel). Therefore, the industry leaders were unanimous in their support of exposure for dairy farmers to governance (Barbara Kuriger) as it means you can then relate your knowledge and life experiences (Jim van der Poel) to your personal dairy farming interests. Mark Townshend spoke of how his governance experiences had helped his personal enterprises:

> I hope that I made a contribution while I was in Fonterra, but the stuff that I learnt during my time there proved you are still learning at 57. I do not think that we would have been able to do the Chile thing as well as we have if I had not been through that experience. I definitely learnt a lot through my time there. (Mark Townshend)

### 4.3.3 Family Dynamics

As the New Zealand dairy industry is historically a family orientated industry, the industry leaders were asked if they believe family dynamics complicate governance. The industry leaders suggest that it does. While the principles of governance are exactly the same (Barbara Kuriger), there are added challenges (John Luxton). These challenges include getting the structures right. In a family situation, if it falls apart it is far worse. Therefore, it’s twice as important that you go in prepared and that you talk about it more (Barbara Kuriger). John Luxton also speaks about the importance of family dynamics. He suggests one of the challenges is if you are employing family, you have to have the relationship that is sound. Chris Kelly suggests the biggest challenge is being careful of nepotism, because amateurs offer little value to a board. This is explained below:

> For example, the husband and wife should not appoint the son and daughter just because they have a son and daughter and want them to be on the board. They should not appoint keen but well-meaning amateurs. It takes some knowledge and understanding of boards and their roles to be a good board member. Someone who does not understand that can be an amateur. No favours. Only experienced directors. (Chris Kelly)

Another challenge is being clear on expectations so that everyone understands what is involved and expected rather than allowing individuals to take a position on the board because they are family. Colin Armer speaks on how his expectations have impacted on his family business:
I have seen too much what I call second or third generation capital squandered, and squandered because the kids don’t have the drive, or governance skills, or the enthusiasm to keep growing things rather than squandering it. One day if they are good enough they might be able to come back and govern this or be involved in the decision-making process for this. So family can benefit. However if I said to our kids, one eighth of this business is yours, just cruise guys, then they will. (Colin Armer)

4.3.4 Effects of the Global Financial Crisis (GFC)

The industry leaders were asked: ‘Did the Global Financial Crisis (GFC) affect your governance model?’ The answers are as follows:

Yes it did actually. I think that it probably made us ask more questions. (Barbara Kuriger)

No, we just sailed right through the GFC. We had good systems in place. The banks had high confidence in our business. We run a no surprise policy. We had all the systems in place for governing and reporting. We can tell you where every last cent has been spent in 13 years in Dairy Holdings. Most people haven’t got last month, let alone 13 years ago. We have excellent recording processes, and high level of confidence with our banks. If you don’t you don’t grow. (Colin Armer)

No, and there is a bit of arrogance in this but I would say because we had such good systems we have cruised through the GFC despite being very highly leveraged. We have been able to grow the business aggressively because we always deliver on what we say to the bank. We have been able to take advantage of the GFC and quality governance would be the main reason for that. Be proactive. (Mark Townshend)

This indicates that a robust governance system will add additional value as it provides stability and security for the enterprise. This adds additional confidence from lending partners, which may allow the enterprise to capitalise on opportunities ahead of other enterprise.

4.4 Board Composition

The industry leaders were asked about the importance of a board’s composition. This was to establish whether a board’s composition affects its ability to add value. The results from this section have been organised into ten sections.

4.4.1 Independent Directors

The industry leaders were asked their opinions regarding the importance of bringing independent directors onto the board. Every industry leader who participated in this research suggested that independent directors are very important to the board’s ability to create value. Henry van der Heyden suggests independent directors bring another dynamic to the board table due to their independent thoughts, independent experiences, [and] a totally different perspective. David Graham suggests that you want independent directors to be smart people, thinking people, people that look at the big
picture. At the end of the day, farmers will not bring everything that you need to the board so that is why you have independents.

The industry leaders were asked what ratio of independents they thought were most appropriate for dairy farm governance. There is no correct ratio, as the board composition will adjust depending to the direction and stage of the business. However, David Graham states *I think more [independents] rather than less is a good thing* while Colin Armer added *the more the merrier.*

### 4.4.2 Woman as Directors

‘Section 2.6.2: Woman as Directors’ identifies previous research which provides evidence to suggest that woman add value to boards. Therefore, this was explored in the interview schedule via the question: ‘do you think female directors add value?’ While the answer is yes, this is conditional. The industry leaders did provide reasons as to why they believe woman add value to a board, but they also provide a reason as to why you shouldn’t put a ‘token’ woman on the board and expect value. The two aspects to this answer are explained below. Firstly, the industry leaders explain that woman add value to a board via diversity. Henry van der Heyden suggests: *woman bring something a male can never have.* Jim van der Poel explains this further when he says *this is because a woman [has] a different set of life experiences* and Chris Kelly thinks that they *focus on slightly different things than men.* This creates a diversity of view which not only is healthy (David Graham) but is *what makes a strong board* (Henry van der Heyden). Value is created via diversity as it *brings a different perspective,* which adds to the robustness of the discussion and the decision-making process (Jim van der Poel)

However, putting a token woman on the board to achieve diversity is not going to work; *if she’s got the wrong skills that’s a waste of time* (Juliet Maclean). Chris Kelly took Juliet’s point further when he was asked the same question:

_I do not think that you should establish a board and say, right I am going to have a four person board. One is going to be a Maori, one is going to be a Samoan, one is going to be a Caucasian and one’s going to be a Woman. That’s what you shouldn’t do. Unless you happen to get those four that happen to be good directors as well._ (Chris Kelly)

Therefore the industry leaders believe *you should select directors based on skills and skill sets only* (Colin Armer) as this will *secure the best candidate as opposed to choosing a woman* (David Graham) because *you always have to go with capability over diversity* (John Wilson).

### 4.4.3 Majority Shareholders

The industry leaders were asked whether they believe majority shareholders should automatically get a seat on the board. There was a divide in the answers with six of the industry leaders saying that majority shareholders should not automatically get a seat on the board. This is because you want the best people on the board if you are to add any value. It has been suggested that *when you go through a process of getting independents or [deciding] who goes on the board you are looking for a capability*
set, and I don’t think that the capability set will be that “I am a majority shareholder” because that’s not a capability (Henry van der Heyden). It was also suggested that these majority shareholders can be restricting. What you’ll find if it’s a majority shareholder they will probably want the right to be on there. But it may or may not be the right decision, depending on where they are in their own career and what sort of personality they have got, because if you think about it from a pure [governance] aspect the board members should be the ones who can create the most value (Jim van der Poel). An industry example is given to explain this point further:

You want competence first. So what scale are we talking about here? In a smaller scale [majority shareholders] should be included. Landcorp do a lot of trade through Ballance Agri Ltd but that should not give them an automatic right to have a director on the board. The Maori Corporations have a lot of shareholding in that form, but they also should not automatically have a position on the Ballance board. You want the best people. That is the problem with an election you do not always get the best people, but you know you have a better chance of that. (David Graham)

You should always go with capability first. It’s who is capable of understanding governance and can operate as a good governor. A majority shareholder should actually want that. If you are a majority or small shareholder it is so irrelevant. The moment that you have a majority shareholder in there thinking as a majority shareholder the business is doomed to failure. Every example that you look at is what happens, I’ve never seen an exception to that. (John Wilson)

The other five industry leaders believe majority shareholders should have the option to be on the board or appoint a seat on the board. This is because majority shareholders own the biggest percentage of the enterprise meaning they carry the greatest risk. One opinion as to why majority shareholders should automatically be on boards is:

They have to be [on the board] because at the end of the day they own the company. Majority shareholders must have an appropriate say on who is on the board. They may want to be represented, or have the right to say what sort of person should be on that board. Now whether they themselves want to go on that board or whether they want to delegate that responsibility to someone else - it is their decision. (Chris Kelly)

Many majority shareholders have it written into their constitution that size allows them to have an appropriate say as to who is on the board. Currently Colin and Dale Armer have the right to one seat with their interests in Dairy Holdings. Although Colin is on the board now, he suggests that this will not always be the case:

Because my shareholding entitles me to a seat, I would or will at the appropriate time resign and appoint someone who in my view will act as an independent but represents Dale and I’s interests as well. (Colin Armer)

Smaller shareholders may feel that they have little say or are being pushed around by their larger counterparts, which Barbara Kuriger believes is probably the thing that is stopping our equity partnerships from succeeding in New Zealand. People go [into equity partnerships] thinking that it is a
good idea and in some cases they are not directors. They find that they haven’t got a say and that they are struggling to grow and all of a sudden it becomes too hard. So a few equity partnerships have gone by the way. However there are ways around this issue:

The smaller shareholders can also have a say. Often the shareholder who has let’s say 51% might have two directors over a total of six. That is one way of dealing with it. Another way is through the shareholders constitution and in that constitution you can say how the majority shareholder has the right of veto or preferential voting rights on certain key elements of that business. So there are ways to have a majority shareholder not having a majority on the board but still having a safeguard. That is the way around it via the constitution. (Chris Kelly)

Mark Townshend’s comment sums up each situation. You need to find a middle ground that works best for the enterprise and its shareholders to create a value adding board.

There is an argument either way. There is a good argument that you want the best people for the job irrespective of the size of their investment. The counter argument is that if you can’t take your biggest shareholders with you then life is going to be pretty hard anyway. (Mark Townshend)

4.4.4 Board Size

The industry leaders were asked about the ideal number of directors to have on a dairy farming board. Responses indicate that the ideal number of people for a dairy farming board should be between three and eight, but no larger than eight. However there is no number or figure that is the best fit. This may be because:

I do not think there is any specific number that works, but it should take into account a number of different aspects around what the business needs. If the owners are part of the governance role [look at] what skills they lack and what skills they actually need to bring on to complement their own skills, to complement the whole decision-making process and the governance process. (Jim van der Poel)

I do not think that there is a figure. Anywhere between four and eight is fine. I don’t think any more than eight is necessary, no matter how big the company is. Any less than four and you are not getting enough diversity on that board. (Chris Kelly)

Juliet Maclean also suggests that there should be no hesitation in adding people to a board to fill these gaps to get the diversity that is needed to add value. Using Synlait Farm’s board as an example: at the moment it is only four and there are a couple of gaps and I think that I would like to appoint someone else to this board. Therefore, it is important to look at what you are trying to achieve and get the right skills to add value and be able to achieve that. For a small enterprise, some of the industry leaders suggest using your professional service providers as these are people you already work with professionally. This is explained below:

If it is quite a small entity you can have a small de facto board with your accountant and husband and wife team. Or either the husband and wife with the farm consultant and the accountant. These people are working with those people professionally anyway and they can
often help with some of those major decisions and it’s often better if you are making those major decisions to involve your farm advisor, your farm accountant and even your lawyer. (John Luxton)

Although many of the industry leaders sit on large boards within the wider industry, large boards are not necessary for dairy farming boards. This is explained:

On the Fonterra board you play a dual role. You have 10,500 farmers that all have a view. So part of the role of the director is actually connecting with the shareholder base. With [only] three or four directors, you would be on the road full time, so you have to get that balance around governance. The fundamental governance will do what governance is there to do, but you also have the softer issues around stakeholder management. (Henry van der Heyden)

Therefore when selecting your board, don’t set out saying you want a certain number of people on your board, rather look for the skill sets and diversity that complete a board to make it whole.

4.4.5 CEO Duality

The industry leaders were asked whether they thought CEO duality, where the CEO and the chairperson are the same person, is a viable option within the New Zealand dairy industry. The majority of the industry leaders suggest this should not happen. There are many reasons for this but they all filtered back to Colin Armer’s point that suggested it won’t work. As that is what governance is all about: separating what is governance and what is management (Colin Armer). The separation of these roles is explained in the following quotes:

The CEO, the person that is actually running the farm, has to sell their case, their budgets, and their capital expenditure requirements. It is quite hard for them to do that when they are chairing and running the meeting at the same time. (Barbara Kuriger)

Having a board adds a good dimension. At Ballance we want the distance between the board and the executive, we want, a healthy tension between the two so that we can ask tough questions and question the decisions that they are getting to. That is what it is about. If you have an Executive Chairman you have a Chief Executive who’s making a recommendation to the board and then supporting it. I think that you lose a bit of that tension. (David Graham)

I do not like that model. I actually think it lacks accountability. I do not even like the CEO or the managing person being on the board. I like complete separation between the board and management otherwise you start to blur those lines. I have quite a strong view around that. (Henry van der Heyden)

There were suggestions that this may work ok on smaller farming businesses (Chris Kelly) where the business has evolved that way (John Luxton). However, all industry leaders suggest that when the business reaches a certain size the two roles should become separate. A potential way for a small business to operate with this variation of this model is explained:

I wouldn’t want them as the same person, so that’s a definite no. Ideally the CEO, the person managing the business, should not sit on the board. However, in a farming business it is not
the end of the world if they do, but they definitely should not be the Chairman. If you are doing that then they should only be one of say five directors. (Chris Kelly)

Therefore, in the ideal situation these two roles should be separate so as to ensure there is a clear separation between governance and management which gives the business accountability.

4.4.6 Revolving Chairperson

This concept is where the chairperson’s role rotates around the directors for an agreed term. The industry leaders were asked what they thought of this idea and how effective it would be in a dairy farming situation. The majority of industry leaders were not a fan of this concept (Chris Kelly). The industry leaders believe that an effective chair requires a certain skill set which not everyone is equipped with, as this role is quite a skill in its own (Chris Kelly). David Graham suggests I don’t think that everybody fits the role of a chairman. You don’t want everyone being a statesman on your board, you want some moderate stirrers that ask different questions and have diversity in the system. Colin Armer is also against this concept. He suggests that the CEO and the Chairman could not establish the necessary relationship due to the revolving structure. Chris Kelly supports Colin Armer’s criticism of this system as it doesn’t allow the chairman to form relationships with senior management, and it also suggests that it goes further than this: A brand new person coming in fresh, not knowing anything about the company, then going straight to chair is quite a challenge. I think that you need at least two or three years for a chairman to understand and get to know the business, the people and get competencies developed (Chris Kelly). Henry van der Heyden supports this and additionally suggests that a revolving chairman would remove accountability.

It is for these reasons that the industry leaders recommend that you should not put rules around it (John Wilson) because no one should get that [chairman] by right (Henry van der Heyden). John Wilson suggests that the board should always make a decision on who the best person to be the chairman is. It was suggested that good boards sit down and work it out, they go through these processes many many times (John Wilson). What sort of board chair does this board actually require? Force the board to have that discussion. What are the criteria, and then measure people against that criteria. (Henry van der Heyden)

However, it was mentioned that a revolving chairperson policy could be a tool for education and training of directors. Jim van der Poel suggests you could do it if it could be part of people’s personal development. Mark Townsend is currently using this model for training. He has recently purchased a farm with a group of young people and while he sits on the board, they rotate the chair in order to develop personal skills. He believes that he could give an argument either way.

Therefore, while the majority of industry leaders believe in having an elected chair, with the right mentoring and leadership, it may be an effective tool for personal development.
4.4.7 Director Election

Industry leaders were asked how they think directors should be elected to the board. There was a clear consensus that directors should be elected by the shareholders, the owners of the enterprise (David Graham). Henry van der Heyden supports this whilst adding this is the fundamental right and role of the shareholder. That should never be taken away. Shareholders should elect directors and remove directors (Henry van der Heyden). Colin Armer provides an alternative example from his association with Dairy Holdings. This company has a small shareholder base, which is an important point to note:

They [directors] are appointed by the board and ratified by the shareholders. Which is in many constitutions. So the chairman would either do a search or ask for advice from the existing board, or go to the old boys network or go through search firms. Say we are looking for a director, get a list of names, interview them, come up with a subcommittee of the board to interview them and the board will appoint. Then at the next AGM the shareholders will confirm with a vote, [minimum] 75%. (Colin Armer)

4.4.8 Selection on Prestige

Industry leaders were asked if they were in favour of selecting directors based on the individual’s prestige. While all interviewees acknowledged this did happen from time to time, they all suggest it was the wrong thing to do (Henry van der Heyden), I am not a fan of that (Chris Kelly) and it is inappropriate (Murray King). This is because you have to be there on your merits…it has to be down to capability (Murray King). Jim van der Poel supports Murray’s comment about capability when he further explains:

I don’t support that. That is not the right criteria, you should pick people because they will add value… I think that you should look at where your company is going, what sort of business it is, what skills it needs, what skills are there already, what skills are missing and how to go about finding those, and the name of that person is secondary for me. (Jim van der Poel)

Therefore when selecting directors the industry must have the best people. And what they are looking for are capabilities and competency and people that can make a difference to their business so they are going to be there to challenge you and challenge your business. They have to be constructive and outwards focused people (John Wilson).

4.4.9 Director Personality Types

‘Section 2.7.1 The Board as a Team’ presented research that categorises directors based on their personalities and the resulting effect on board efficiency. To establish whether the industry leaders believe that personality types have an effect on boards, the following question was asked: Do certain personality types add or detract value?

The industry leaders suggest that while some individuals may not be suited to be directors, you still need different personality types to create a robust, dynamic and effective board. This is because if you
select your mate you put on the same sort of person with the same sort of thinking, which is parallel thinking rather than diversity (David Graham). Thus in order to have this value creating board you must allow careful selection of people who will work as a team (John Luxton).

Colin Armer suggests that personality types are less of an issue. Rather than being personality focused there is a more basic thing and that is integrity. *If someone has good integrity that shows up, [they] stand by their principles. If they think, something is not right they say so. I have seen people accept decisions that they do not believe in, but the warm seat feels better* (Colin Armer).

Therefore it is important to get a mix of people to be directors and that they are there for the right reasons, and this will then add value.

### 4.4.10 Training for Directors

Popular media and publications have indicated that there is an increase in people wanting to be a director within New Zealand (Institute of Directors, 2013). The industry leaders were asked for their views on what was required for an individual to be a good director.

Many of the industry leaders thought that it was up to an individual to take the initial step. Henry van der Heyden suggested that this was as simple as putting yourself forward:

> Why don’t [farmers] develop themselves and actually make themselves available for a board? It would broaden their thinking. It is easy to start out and get on a board even if you just get on a local school Board of Trustees. (Henry van der Heyden)

Another approach is for those currently in governance positions to take young ‘up and coming’ individuals under their wing in order to educate the future generation. This is currently being done both at a farm level and at a wider industry level. This is explained in the following quotes:

> Most of them [farm managers] have really good ideas, they just have to learn the boundaries between governance and management. That is our role, as the people who have done it before them. We actually guide them through that, for example we teach them what an agenda is and show them how to run a meeting, because everybody’s input is valuable. (Barbara Kuriger)

> We have one first time director on our board. That person is there for experience. One out of eight is no big deal. I think that is important for that particular board and for their own future development. (Chris Kelly)

While the following quote is a summary of all the above, it also explains the pathway of the selected industry leaders into their directorship roles:

> There is no substitute for getting your hands dirty. Get out there when you are young. Be involved in your own business, involved in all the successes and failures and the highs and lows. [You learn] the huge satisfaction when you get it right and being able to respond quickly when things are not going so well. Building that over a decade or two is what makes people
good directors. It is that invisible framework; from being educated well, being brought up in an environment where you have good values, which is actually the most important thing by the way. Good values, honest ethics, which gets you 80% of the way. The next 18% is life experience and the last 2% is formal training. So going into a Institute of Directors (IOD) course is the bit on the top that brings the framework from life experiences together. My experience would be too many young people are thinking, I want to be a director, I want to be a governor of these organisations. Wrong answer. What you want to do is go and get your hands dirty, earn respect, learn from your mistakes and build up experience over time. Then you will have the potential to be a very good director. (John Wilson)

4.5 Board Meetings

A board meeting is often referred to as the black box (Huse, 2007). This is because nobody aside from those involved actually know what happens in a board meeting. Thus, the industry leaders were asked some basic questions. This has been divided into six sections.

4.5.1 Level of Formality

The industry leaders were asked how formalised they believe these dairy farm board meetings should be, regardless of the size of the business in question. There was a unanimous response that a high level of formality should be upheld, because this is how boards add value (Henry van der Heyden).

It was suggested that meetings should always be held around a board table with all members present. This is because you want the formality of going through the agenda, the formality of the discussion that goes with it, and different things (David Graham). While many boards hold conference calls this was not advised as you have to be face to face if you want to get something done and that’s because I read the people (Colin Armer).

If you make it so the board meeting is of uttermost importance and people get nervous then it’s like a rugby test match. You do not play a test match in the back park, you have got to take it to that level. (Henry van der Heyden)

You should sit down around the table and have the formality of reports that comes out to you from the Executive. We at Ballance go around to our different plants around New Zealand, it is good for directors to see what is going on at different plants. Also to meet the senior staff, it’s good for morale and the boards education and that sort of stuff. However, you want the formality of going through the agenda, the formality of the discussion that goes with it, and different things. So the board needs to sit down, but it is not unimportant to be out there looking at what’s going on as it changes your views sometimes. (David Graham)

We will always have someone there to take the minutes. I then ask the minutes to be sent to me first. As chair, I double-check them first to see if I think that they are reflective of where we got to and the decisions that we made. To me the board minutes should be a reflection of the discussion, it should be just picking up the key points. I don’t like minutes that say "John said this" and "Brett thought that". I think that they are a waste of time, they are just muddily. I like them to say the board had a discussion around investment and the action is this. Therefore, when you reflect on them they say this is the discussion and this is the action that came out of
them. In the beginning of each board meeting we go back through the action list of the previous meeting. (Jim van der Poel)

The above quotes show a high level of formality is needed for the governance of dairy farming enterprises. By having formal processes across the whole enterprise a level of professionalism is added to the enterprise. This will also mean that there is a higher degree of accountability which should protect the enterprise.

4.5.2 Regularity of Meetings

The industry leaders were asked how often they believe that board meetings need to be held. The industry leaders spoke in general and referred to interests in which they are involved. Regularity ranged from about ten times a year (Chris Kelly), six to eight, it depends on the size of the business (Henry van der Heyden), every two months (Jim van der Poel) I think that you can quite successfully [hold meetings], quarterly (Barbara Kuriger), to four board meetings a year (Colin Armer).

4.5.3 Preparation for Meetings

The industry leaders were asked what preparation they would expect of an individual before a board meeting. All industry leaders suggested that a director must be fully briefed (Colin Armer) before entering the boardroom. The industry leaders stated that a good board will get the board papers at least a week before the meeting. This allows time to read them thoroughly and understand them (Colin Armer) and get a feel for the business (Henry van der Heyden). This also allows a director to do some homework on issues (Jim van der Poel) and allow them to turn up with their own perspective (Henry van der Heyden). This is important if a board is to achieve a value adding discussion because you come with a view but also an open mind. You cannot just form a view based on the discussion around the table: you have to have a view. You just cannot come without a view listen to what everybody says pick up the best discussion and go with that (Jim van der Poel). You cannot turn up and think that you are going to wing it, because you get caught, you will be seen straight through. It is like any meeting that you turn up unprepared for and you will lose creditability quickly (Murray King).

4.5.4 Topics of Discussion

The directors were asked, what should be the topics of discussion at dairy farm board meetings. Many of the industry leaders spoke of board topics of discussion as sections (Chris Kelly). The industry leaders recommend that strategy is number one and out there by a long way (David Graham). The following quote gives a breakdown of board room discussion:

We break the board meetings into four or five sections. The first section of the board pack is about strategic issues. We just discuss with all the directors the big strategic things we are doing. The second section is about items requiring formal board resolution. We might say we want to buy a farm in Southland worth ‘x amount’, here is the business case and we would like approval to spend ten million to buy the farm. The third section is the section for information, that is always the financial section, and that is all about how we are tracking against budget
and the sorts. The fourth section is all about how farming is going at present, how the drought is affecting us, how the people are feeling, all those sorts of things. That is a standard format that we use. Most other boards have a similar format that they use. (Chris Kelly)

4.5.5 Voting

The industry leaders were asked how they go about reaching a decision as a board. It was suggested that you never really want to vote (David Graham). Rather, if you can get a decision by consensus then that’s better. This then means that the board is aligned (Juliet Maclean). Therefore, when making a decision everyone is behind that decision. If you have a board where everybody doesn’t get behind that decision once it’s made, then you have got trouble. It will fall apart. So consensus, you have got to have it, otherwise you disintegrate (David Graham).

4.5.6 Reporting from Management

The industry leaders were asked what reporting they require from management. The responses suggest that the information should be timely and relevant if the board is to make an informed decision. This is explained in further detail in the quotes below:

*The managers’ report monthly. We have a very structured financial and physical reporting template which the farm managers’ reports feed into. It is done in a formal way. It is shared with the board, the managers and our other stakeholders. It is a routine that we just stick to very rigorously.* (Juliet Maclean)

*I am a bit of a control freak. I’m not saying it’s right or wrong, it’s just a personality type. I am actively involved and communicating with management to make sure that things are on target. The pure model is giving the management absolute free rope, which is what should happen in a perfect world; the governors are governors and the managers are managers. But if you have too much rope I think that you then have a high risk of a) the company suffers because it’s not quite done right or b) you end up having to kill your manager or your CEO because they have made a mistake. I guess when you get older or more experienced you can see the mistakes as they come.* (Mark Townsend)

*The chairman and the manager get around most farms regularly. We have very up to date accounts coming through the system as well. We are very aware of what’s happening.* (John Luxton)

*The key role of the board is value creation so you have to have a value creation metric. With most of our farms we really are looking to grow EBITDA so you need some financial metrics.* (Henry van der Heyden)

A detailed monthly report from managers is suggested as an informative reporting tool. This should include a financial metrics of the farm accounts. If this is stuck to rigorously it allows information to flow between management and the board. It was also suggested that there should be active communication between the board and management to ensure that they are aware of what is happening and targets are achieved. In a farming context it is suggested that the manager and the chairman get
around the farms on a regular basis for visual analysis between the farm reports and the farm operation.

4.6 Strategy and Vision

The industry leaders were asked about board roles in relation to strategy and vision. This has been separated into the following four sections: Setting strategy and vision, reviewing strategy, maintaining control of strategy and advisory boards involvement in strategy.

4.6.1 Setting Strategy and Vision

The industry leaders were asked how they believe directors develop strategy and vision for the business. First, the industry leaders stated the importance of selecting individuals to be directors who have the right aptitude for business. Colin Armer explains:

> You have it or you have not. Someone who has not had a plan for thirty years putting them on a board as a director isn’t going to change them is it? You are not going to appoint a director that has no views on life and is not going forward. So I think if someone appoints me to a board they will assume I have already got that view. I do not think that people should get to a board if they do not have a view on certain things. They should have a view on creating wealth and investing and growing. (Colin Armer)

It was then suggested that directors need to spend time getting to know the company (Chris Kelly). This can be achieved by site visits (David Graham), being well read (John Luxton), or short placements or days with management (Chris Kelly). The following quotes provide further suggestions.

> I do not think that directors develop [strategy and vision], I think that is the executives’ responsibility as they are the people that are inside the business running it. Executives should develop the strategy and then they should present that to the board in a structured way. I think that is where it should come from, but it is our role as a board to quiz the executives hard on that strategy. We are looking to see if this is the right direction and giving our insights as farmers and independents about the correctness of it. Then the executives need to go away and put that in place. So it’s still the strategy but they will work on prongs of it then they will come back to meetings and re-present that particular part of the strategy. Strategy becomes a big part of your board meeting and should be the focus of your board meeting, the rest becomes sort of second. Then annually it rolls over and we go, have we got it right? Is this the right thinking? (David Graham)

> I think being very widely read is important. You have to look at things in the context of a changing world and I think that that is often a problem that the farming community has. As individual farmers we tend to be on our farm and very busy and perhaps not hooked into the wider world and some of the macro changes. (John Luxton)

This suggests that a director should not be appointed to the board unless they already have a view on strategy and wealth creation. A director must be constantly updating their view as dairy farming enterprises operate in the context of a changing world. If directors do not do this then they will not be
able to support management in offering relevant feedback when management present the board with strategy.

### 4.6.2 Reviewing Strategy

The industry leaders were asked how often the strategy should be reviewed. The answers are as follows:

> There is always the saying that if you have an equity partnership, once in every five years something happens in someone’s life. When you have a few partners and a few directors, you have to be constantly monitoring. People’s needs change: someone will have a baby, someone might die, marriage breakups happen. I think that it’s constantly being in tune with what’s going on with the people as much as anything. (Barbara Kuriger)

> [With strategy] there is on-going review. (Juliet Maclean)

This suggests that strategy should be reviewed on a regular basis. The environment in which the enterprise is operating is constantly changing and so too is the objectives of those who own the enterprise.

### 4.6.3 Maintaining Control of Strategy

The industry leaders were asked how to ensure that the strategy is maintained due to the managers having the day to day control of the operation, which is an issue due to the separation of ownership and control. The suggestions included:

> I use a team briefing approach. Let’s pretend we have had a board meeting today. I write up a team brief of the board meeting. If it is a strategy day, we will say these are the new strategic initiatives. I then get all the staff here involved and talk to them, and give them a download on the board meeting. Their staff go away and talk to their staff, and it cascades down onto the farm. Secondly, either every year we have a farm business manager’s conference or every alternative year a group of us go around the regions and talk strategy to all our staff. It is really important that you do it as it is more likely to stick if you personally connect. However, the more you communicate the more people want you to communicate. So it becomes a vicious circle if you are not careful. They just want to hear from you. We also have our vision and things like that are pretty visible. (Chris Kelly)

> Ultimately, the board has the power to hire and fire the Chief Executive. And good management understand that. (Henry van der Heyden)

> First thing is employ the right people: if in doubt do not hire. Employ on attitude so that’s the people with the right view of the world and that doesn’t matter if they don’t have all the right skills as long as they are prepared to learn and ask, that’s all you need. (Murray King)

> It is a very disciplined process. We have a very outstanding CEO but it is his job. He is paid bloody well but he has about a third of his wage at risk, which is tied to performance. Some of it is about trust, some of it is about the quality of the person and some of it is where you put the carrots. (Mark Townshend)
These quotes indicate that it should be a disciplined process. Initially, if the correct people are hired in senior management they will have the ability to communicate a concept in a manner in which others want to follow. If a concept is communicated in person from senior management it means it is visual, which allows greater buy in as it filters down through the company. However, if senior management are acting in a wayward manner that is not aligned with the company, the board has the ability to remove them and replace them with someone suitable.

4.6.4 Advisory Boards Involvement in Strategy

The industry leaders were asked what they thought of using an advisory board to help the board in the creation of strategy. It was suggested that an advisory board should not be used as a tool to help create strategy. This was because you need those who are to implement the strategy to be part of the process, if they are to add any value in appointing it. This is further explained in the quote below:

> What is important here is that if you have a strategy you own it. It is yours and it reflects what you want to achieve and how you are going to get there. If you have other people help you articulate and get to this position, if you are not good at that yourself, that is fine. However, I do not think that anybody else can write a strategy for you. While you often find that company’s employ consulting groups to come and write their strategy, I am never convinced about this, because anyone can write a good strategy but the value is not created in writing the strategy, the value is created in appointing it. You only get a fighting chance of getting good implementation if you get buy in from the people. If the people that will implement the strategy are part of the process, you get more ownership. So if you have got a farmer who wants to develop a strategy, having someone help them get out what they want, how they want to get there and where they want to go is helpful. However, if they write it for the farmer then they just lessen his chance of being successful. (Jim van der Poel)

For this reason the industry leaders suggest that an advisory board should not be used as a tool to create strategy. It was also suggested that if there is a good working relationship between the executive team and the board there should be no need for both: *For our business, I don’t see that you should need a board and an advisory board. I can’t think of a set of circumstance where both might be necessary* (Juliet Maclean).

4.7 Exit, Entry and the Shareholders Agreement

The industry leaders were asked how they thought the entry and exit of shareholders should be handled and about the importance of the shareholders agreement. This has been split into two sections.

4.7.1 The Shareholders Agreement

The industry leaders were asked how importantly they viewed the shareholders agreement. All industry leaders said this was of utmost importance, with explanations below as to why:

> This is critical. This needs to be professionally done. We had a shareholders agreement in Dairy Holdings which nobody took any notice of for ten years. Then for convenience sake most of the other shareholders lost their copies and denied it ever existed. We plucked our one
out of the cobwebs and said, it does exist because these are all your signatures and this is the way it runs. You would probably have read a bit about that in the media. They tried to run Dale and me over, because they wanted to sell the whole company. We said no, no we are staying here. They tried every dirty trick in the book to run us over but it didn’t happen because we had the shareholders agreement. We had the comfort of that and in the end they had to do what the shareholders agreement said. (Colin Armer)

Having a good shareholder agreement is absolutely important. We have good protections in place for minority shareholders or majority players, which were put in place before I bought into the company. (John Luxton)

As explained in the above quotes, a shareholders agreement is a legal document which all parties must agree upon before it is signed. In doing so, clarity is given regarding a number of issues. If an issue comes to light, this allows all parties to act upon the agreement. This provides clarity, while also handing the issue in a approach set out before emotions became involved.

### 4.7.2 Exit Requirements and Exit of Capital

The industry leaders where asked how they suggest a board should handle the exit of individuals and capital from an enterprise. It was suggested that there should be an initial lock-in period to allow the board to set a strategy that will not be affected by the change in partners or capital availability. If a partner was looking to leave there should be a notification time slot so the enterprise is not disrupted during busy periods. If a break up does occur this is when the shareholders agreement is followed. By following a pre-emptive agreement relationships are less likely to come under pressure. This is explained in further detail in the following quotes:

*I think that for a start you need a lock-in period. So you don’t do all the work then tip the thing on its head in the first year. So maybe that’s three years or five years. After that you just have to give notice. I think probably the easiest is by a certain date each year. You know the time that certain things happen each year like after calving, after mating, and things are starting to taper off so November-December. You have to give notice by November 1st and you probably have to have a cut-off date so if you can’t make something work by the end of March or February it becomes too late to start a restructure. So that’s what I would be looking for.* (David Graham)

*Spectrum partners have been in partnership for 16 years. Not only have we got a long history of a working relationship, but we have also become friends along the way. It’s important that everyone is treated fairly and equally, it’s important that the personal aspect is preserved so there is nothing in this process that destroys that relationship that you have with the other people. It’s important that when the restructuring is done nobody is disadvantaged, everybody should have equal opportunity to make their share of what they have left be successful. It’s ultimately in their hands as to what they do with it next but at the transition everybody has equal opportunity to be successful with what they’ve got. And so that’s what we are trying to achieve.* (Jim Van Der Poel)
This shows that there needs to be considerable time spent looking at the details of any partnership. In turn this will protect the organisation for all parties. When people ask me what is the most important part of my job, it’s to protect the organisation (John Wilson).

4.8 Future Challenges for Dairy Farming Boards

The participants were asked what they thought will be the biggest challenge dairy farming boards will face in the future. The results have been sorted into these categories: ‘transition’, ‘compliance’, ‘capital and productivity’ and ‘governance success’.

Transition

This section suggests that the future challenges faced by the industry are associated with the transition period. This refers to transitioning one generation from actively farming to the next into farm ownership. It also includes the transition of shareholders as the business evolves: whether this be due to events such as divorce or succession.

The next generation. Finding the right people to partner with. Giving the younger generation the opportunity to grow, and giving them the opportunity to transition through until you are completely out of it. I think that is the biggest gap that we have in our industry, is how to bring that next person through and transition them through until they own it. And that’s what it’s all about. For me transition is really exciting. I’ve always found that it is really important to never forget where you have come from and I would like to continue that in New Zealand. All our generation know how we got started, it’s generally because someone else gave us an opportunity and I just want to see that continue. (Barbara Kuriger)

I actually think it is a liquidity event. It is actually the exit of the shareholders and then it is succession. Succession is bloody important. I don’t know where I would put the weighting between the two. But it’s those two. (Henry van der Heyden)

Divergence of interests of shareholders probably. In human nature, people change. They grow, they evolve, they have different needs, they die, they divorce, they do all sorts of different things and so it’s just human nature. These challenges are always going to be a moving thing as nothing ever stays the same and they are always going to have other risks that they are dealing with and challenge... that’s what the nature of farming is all about anyway, it’s dynamic and ever changing. (Murray King)

Compliance

The industry leaders suggested that future challenges faced by the industry are associated with compliance. As the industry is required to meet a higher level of compliance the board faces the issue of becoming more like an auditor rather than a value creator.

I think compliances issues will be enormous. Making sure that we keep the company out of jail because of effluent problems or animal welfare problem and that sort of thing. So what they are going to face is a conundrum between being too prescriptive as a board and making sure that there are no problems, no issues with compliance on the one hand. So boards becoming really sort of like auditor where you really have to dot your i’s and cross your t’s. Through to the other side, where having enough experience [is needed] to be able to create value for the
company by doing new things, and there is always a bit of tension between those two. (Chris Kelly)

Capital and Productivity
Leaders suggested that the future challenges faced by the industry are associated with capital and productivity. This is because dairy farming is a capital intensive industry and profitability is dependent on factors outside the farmers control, such as environmental and economic constraints.

It’s the lack of profitability. Costs rise to meet the milk price - worldwide. If you look around the world, it’s one of the things that I did learn at Fonterra, is that no matter where you are in the world the costs rise to meet the milk price, and so a dairy farm’s margins and profits gets squeezed. (Colin Armer)

It’s a capital intensive industry. I don’t think that prices can go up a long way so we aren’t going to get capital gain to any degree, so you are going to have to run the farm and run it financially well. There are some real risks around exchange I think and interest rates. Interest rates are low and they wont stay low. So it’s the financial management. I think it is going to be quite tricky on farms going forward without any capital gain. And these big units, how to manage them. Finding the skill and the right people to manage them. And that takes you into a structure where it is equity ownership or contract and sharemilkers or combinations or whatever. So to me it is the financial side as the risks are high, with higher payout and higher indebtedness and the industry short of good people to manage farms. (David Graham)

I think capital will be a big challenge for the industry. I think that we are a bit over-capitalised. But then internationally I think that people want a chunk of our industry, so it is still a very good place to be. (John Luxton)

Governance Success
This section suggests that the industry shouldn’t face any substantial future challenges if the right level of governance is correctly applied to the enterprise in question.

I don’t think that there are challenges there if [businesses] are well governed. I mean the most important job that a board does is actually appoint your manager or your CEO. So if you have good governance [you are] sorting out strategy, overseeing budget processes, approving budget and monitoring performance through the year. I don’t see any challenges, it’s just a process. As long as you are appointing the right CEO it’s simple. (Mark Townshend)

It’s the conversation that you and I have just had. It is getting the governance right and then it will all flow underneath it. So it is about answering all the questions that you have just asked me. (John Wilson)

I get very clear feedback from my banking syndicate that 70% of dairy farming businesses don’t run a budget. [So] just don’t kid yourself that you should start with governance if you can’t get your financial reporting right. So my very personal opinion at the moment is that there is way too much focus on governance when the basics aren’t even sorted out yet. (Juliet Maclean)
4.9 Board Operating Models

This concept is drawn from the literature and explained under ‘section 2.7.2’. As explained, boards will slide back and forth across this continuum (Nadler, 2004). However, gaining an understanding of where a board is usually situated along this continuum will allow the board to implement best practice to achieve greater productivity and efficiency (Carver, 2003; SPARC, 2009). Thus the participants were presented with this continuum (see p. 21) and asked to select the point at which they believed the board would operate most effectively.

One hundred per cent of participants agreed in stating that the ‘Engaged Board’ was the position where a board would operate most effectively. Murray King suggested this would be my choice, [The Engaged Board] because at the end of the day you get the best out of people when you help them, not when you control them. Many participants indicated that this would be their choice because they liked the terminology suggesting that the board is the CEOs partner, which reflects stewardship theory.

While all participants did state that the ‘Engaged Board’ was the most effective, it was suggested that there was a need for some of the other operating models. Juliet Maclean and Chris Kelly stated that there was a need for the ‘Operating Board’ in times of crisis or intensive change. Mark Townshend and Chris Kelly also noted that the ‘Certifying Management Board’ can be effective in a stable company, however this depends on the risk profile of the company, its maturity and where it is at (Chris Kelly). Lastly, no participant believed there was ever a time that the passive board would be most effective. Barbara Kuriger and Henry van der Heyden point out that this is because a board should never have limited accountability.
Chapter 5
DISCUSSION

5.1 Introduction
The purpose of this chapter is to compare and contrast the industry leaders’ perspectives to the literature in order to answer the research questions proposed in chapter 3 and to present conclusions for this thesis. Section 5.2 presents a model of dairy farm governance adjusted from the research findings. The content of section 5.3 includes an insight into the selected corporate governance theories, and analysis to suggest the relevance to this study. Section 5.4 discusses the board roles, and section 5.5 looks at board composition. Section 5.6 discusses ownership considerations, and section 5.7 reflects on board dynamics. This is followed by the answers to the specific research questions (5.8), then the discussion is concluded in section 5.9. Section 5.10 discusses the contribution to the body of knowledge. Section 5.11 discusses future research potential and section 5.12 the limitations of this research.

5.2 Adjusted Governance Model
The research proposed a model for dairy farm governance from the literature reviewed (section 2.9). The research findings presented in chapter 4 suggest that this model needs further development to be a useful representation of dairy farm governance (see Figure 5-1). The research identified two major changes to the proposed model for dairy farm governance.

Finding 1
The first major change to the model is the addition of the overarching arrow. This indicates that when looking to establish dairy farm governance you must first consider both the ownership and operational structures of the business. It is critical that this analysis is completed before looking at board factors as this will ensure the level of governance is appropriate.

Finding 2
The second major change to this model is an alteration to the board roles section. It was identified that control is the most prominent of the three roles due to the intimate relationship of farmers and their businesses. The business is often their home and if they are delegating governance, the research indicates that they still require a high level of control. Thus, the control concept has increased in size. The control role, however, continues to overlap with the strategy and service roles, which indicates that these roles are in an interconnected relationship.
Figure 5-1 Adjusted governance model for New Zealand dairy farming enterprises
5.3 Governance Theories

The literature review identified four different theories that could be applicable for dairy farm governance research. These theories are agency theory, stewardship theory, stakeholder theory and resource dependency theory.

Agency theory “is directed at the ubiquitous agency relationship, in which one party (the principal) delegates work to another (the agent), who performs that work” (Eisenhardt, 1989a, p. 58). This delegation creates a separation of ownership and control (Berle & Means, 1932). The literature review identifies two main agency problems that are common. The first problem arises when the desired goals of the principal and the agent conflict while the second agency problem is that of risk sharing. The industry leaders note that issues surrounding control over farm management is a very common problem within the New Zealand dairy industry. The industry has seen a change in ownership composition, which has increased the number of corporate farms and other ownership models where there is a separation of ownership and control (Kelly, 2012). In these cases the principal delegates the work to the agent to perform. An industry example of agency theory in practice can be observed through the relationship of a contract milker and a farm owner. A contract milker is paid on a rate per Kg/MS produced. The contract milker may try to maximise production with no regard to the cost of production. Therefore the first agency problem of control may occur through the contract milker’s actions of maximising production versus cost efficiency. While the principal will have the desired goal of running the most cost efficient system (Mark Townshend), an agent may select options that increase their own utility. However, given that the principal relies on agents to run the organisation, the agents end up with substantial residual control rights, and therefore discretion over how to allocate investor funds. This means they are more likely to be able to act on their own goals. A second agency problem is risk sharing. Risk sharing arises when the principal and the agent have different attitudes towards risk, which influences their actions. The literature suggests this includes areas such as compensation, regulation, impression management, whistle-blowing, vertical integration and transfer pricing (Agrawal & Knoeber, 1996, p. 379). The industry leaders suggest that managing this relationship can be a challenge (Barbara Kuriger). The literature suggests that a board of directors is one of the mechanisms used to control these agency problems (Dulewicz & Herbert, 2004; Pettigrew, 1992). This can be effective as the board adds a separate level that is independent from management. Under agency theory prescriptions, the board’s main role is to ensure the agent acts within the interests of the shareholders. Thus, the board would help reign in this behaviour and ensure that the business operates effectively. Barbara Kuriger echoes Pettigrew and McNulty (1998) when she suggests, that in a farming situation the ‘[agent’] should submit a budget to the board for approval at the start of the business year. This will act as a control. One tool noted by an industry leader was to use incentives (David Graham) to align behaviour. While Henry van der Heyden adds that, this is how a board adds value as they can hold the person running your business to account, which will de-risk the business.
Therefore as it is the board’s job to keep the agent aligned with the principal, an agent should remember the board has the power to hire and fire (Henry van der Heyden).

Stewardship theory contrasts with agency theory (Daily, Dalton, & Cannella, 2003; Muth & Donaldson, 1998). Lane, Cannella and Lunatkin (1998) state that stewardship theorists believe that the stewards’ interests are often aligned with those of the shareholders. Therefore, this theory suggests that a board’s main role is to support the manager. Under this theory the manager would also be on the board. An analysis of the data received from the industry leaders, suggests that it is a very common situation within the industry. Barbara Kuriger provides some support for the application of stewardship theory, giving an example of an equity manager on a farm. This equity manager is on the board, which is quite important as they are the one out there running the farm on a daily basis (Barbara Kuriger). She then suggests the rest of the board should include other shareholders, independents, and directors with banking or finance skills (such as the accountant). These other directors surround [the manager] because if they do well, everyone does well and they are the ones driving the business forward (Barbara Kuriger). The industry leaders also suggest that management are more likely to align themselves with the other shareholders in their objective to get the best from the company, if they are a part of board discussion. A board provides the platform for a robust discussion (Murray King) which is more likely to result in a collective agreement by all parties. The industry leaders also note that employment of like-minded individuals is important. You want to employ people who have the same interests, rather than having to incentivise by other means. If you have to be there all day standing over people to get something done, then something is wrong (Jim van der Poel). If in doubt don’t hire (Murray King) because if you [hire] the right person your life will be a breeze (David Graham). The industry leaders note that clear communication is vital so that this relationship maintains its effectiveness. The industry leaders suggest that stewardship principles allow an advantage to the enterprise as the board of directors have a workforce which is pro-organisational in their working manner. If you achieve this, then it is very easy. They have a job to do and you can let them do it (David Graham).

Stakeholder theory suggests that enterprises have relationships or ties that impact on a wider group of people and that there is value and benefit in these relationships for the enterprise (Hill & Jones, 1992). This theory suggests that stakeholders, such as ECAN or Mighty River Power, should have positions on the board, so that their view is taken into consideration for decision-making. However, the industry leaders were not in support of the implications of this theory. These stakeholders could be motivated by their own agenda or viewpoint, which means they can be restricting (Jim van der Poel). The industry leaders suggest that it is better to focus on attracting directors that can add value to your business, some of whom will understand the wider agricultural sector (John Luxton). These directors should have the ability to handle these external relationships and contracts, without having a negative
impact on the enterprise as there are a multitude of inputs with no one single input being critical to success.

Resource dependency theory suggests that a board of directors is a channel through which additional external resources can be obtained or acquired by their organisation (Pfeffer & Salancik, 1978). Thus under this theory members of the board are appointed to bring critical external resources to the firm, which are used to enhance the enterprise’s prestige, reputation and legitimacy. The industry leaders suggest that this theory is not applicable to dairy farm governance.

5.3.1 Theory Summary

This section discussed how the theories utilised in corporate governance research apply to dairy farming governance within a New Zealand context. Of the four theories, agency theory and stewardship theory have explanatory power. This was due to the impact that ownership and operational considerations have on the business model, which in turn places control as the most important of the three board roles. Neither stakeholder theory or resource dependency theory were considered relevant as there was no support for their considerations by the industry leaders. The implications of this suggest that it is critical to the successes of a governance model to take time in appointing individuals to roles that best suit the direction of the enterprise.

Having the knowledge of these theories and actively observing if these theories are relevant to the enterprise in question, will allow future research to observe the strengths and weaknesses.

5.4 Roles of Boards and their Directors

The literature review identified strategy, control and service as the three underpinning roles of governance. In a dairy farming context the same three roles have been identified. However the three roles do not have an equal level of importance, as explained below.

5.4.1 Strategy

The literature review shows that the strategy role is a fundamental underpinning of governance (Huse, 2007). This is because the strategic role taken by the board leads to the direction that an enterprise pursues. To achieve long-term results and survival, a board must have the ability to direct executive attention towards strategic decision-making as this is the cornerstone of effective strategy (Huse, 2007). Eisenhardt (1999) offers three ways in which a board may be involved in strategy: legalistic, review and analysis, and partnership.

Industry leaders suggest the relationship between the board, the executives and strategy should never be legalistic or a partnership but a mix of review and analysis. The primary reason that a legalistic approach is not favoured is because a board’s responsibility is to the company first. As noted by Colin
Armer - a director must focus on the company first and then ultimately that will benefit the shareholders, but this should never be the other way around. The industry leaders also note that a partnership approach is not suitable. If a director was to initiate and develop strategic changes instead of approving managerial choices, they would be blurring the lines between governance and management. Therefore this is not achieving what governance is all about: separating what is governance and what is management (Colin Armer). For these reasons, review and analysis is the most effective approach for the board to support the management team in setting sustainable and value-adding strategies. However their role should be restricted to the review and analysis and sign-off of management proposals. This approach allows the board and the executive team to work effectively to steer a business in the right direction.

The literature suggests that the board must first master four key areas before they can effectively review strategy, which are stage setting, stimulation, discipline and defusing (Stiles & Taylor, 2006). These four areas have all been noted by the industry leaders within the research discussion. Although these findings would indicate that the industry leaders place strategy as their number one concern within the board room this cannot occur unless the board has control.

**5.4.2 Control**

Control can be seen as a question of “who has basic control over key decisions?” (Huse, 2007, p. 247). While this is seen as one of the fundamental elements of governance, this research suggests that passing control to a board may be the biggest deterrent to implementing governance for dairy farming enterprises. As agency theory explains, when the work is delegated to the agent, the principal loses an element of control. The industry leaders note that in some cases we have not done this [implemented governance] because I like to be in control (Murray King). However when the principal or shareholder passes control to a board, the board becomes legally accountable for all decisions made within the enterprise. Therefore, the board is taking on the responsibility of approving key decisions within the enterprise that are aimed at the success of the company. The board is given this responsibility of protecting the interests of the shareholders by controlling the actions of management, so that illogical decisions are not acted upon and opportunistic management styles are kept to a minimum.

Control in an enterprise is implemented effectively via different monitoring systems, such as committee meetings and continual assessment of managerial abilities. This provides the board with the transparency they require to observe the running of their enterprise. The industry leaders explain that a board needs very structured financial and physical reporting (Juliet Maclean) which is timely [so] we are very aware of what’s happening (John Luxton). This is because control is not achieved by a single act, but rather an accumulation of multiple different actions.
5.4.3 Service

The literature suggests that the board provides a service at the institutional level within an enterprise. The board achieves this role by providing advice and counsel to senior management. They do this by accumulating all their skills, knowledge and experience into a combined resource, then using this resource to assist the enterprise. This service can be provided internally within the enterprise by guiding and advising the CEO and senior management, or externally by bringing in associates or contacts to advise and use their prestige as directors to increase the reputation of the enterprise (Huse, 2007).

The industry leaders said this role is especially important to dairy farming enterprises as it is not often that any individual, such as a farm manager, has all the necessary skills. Therefore this is an area where a board is able to create value as they have the ability to fill the gaps in competency and knowledge. It is for this reason that the industry leaders suggest due care must be taken in the selection of directors. They state that you must take the process of selecting directors seriously and not select friends, acquaintances or people on their reputation alone – unless they also have the skill set that is required.

5.4.4 Summary

This section discusses how the three widely agreed roles of board governance; strategy, control and service, operate within a New Zealand dairy farming context. While it was found that these three roles are important and need to be considered if a board is to add value, one role was identified as being more important than the others. This is the board role of control, as shown by its enlarged sphere in Figure 5-1. Control has the largest effect over board behaviour. This affects the other two roles because if control is not addressed, the board’s ability to set strategy and provide service is compromised.

5.5 Board Composition

As indicated in the literature review, an element of sustained competitive advantage lies not only in access to finance or capital, but also within an organisation’s board (Barney, 1991; Lundy, 1994). The results chapter of this thesis supports this, with slight modifications within the context of dairy farming as outlined below.

5.5.1 Independent Directors

An independent director is a director who has “no personal or professional relationship to the firm or firm management” (Daily, McDougall, Covin, & Dalton, 2002, p. 229). Previous researchers provide contradictory evidence about the value of an independent director in the governance of different enterprises (Amoako-Adu & Smith, 1995; Zahra & Pearce, 1989). However the industry leaders in this study expressed only the positive value of independent directors in dairy farm governance.
The industry leaders state that the positive value brought to a board via independent directors is created due to added diversity. This diversity comes in the form of different experiences, ideas and viewpoints (Jim van der Poel) that help shape an individual’s actions. By having these differences, a board has greater ability to conduct robust discussions and make better decisions.

It was also suggested that independent directors are less likely to be swayed by personal agendas. As these individuals have no personal or financial relationship to the firm, their view is less likely to be biased (Colin Armer) for personal advantage.

5.5.2 Majority Shareholders

Research has suggested that majority shareholders often demand to be on boards (Huse, 2007), which may or may not add value to the enterprise. The industry leaders state that majority shareholders should only be on the board if they are capable of enhancing the value of the entity. However, consistent with the literature they suggest that majority shareholders often demand to be on the board. In section 4.4.3 the industry leaders suggest ways of dealing with this issue while still achieving value creation. This includes controls such as ‘one seat one vote’, independent directors, and appointment to the board by election only.

5.5.3 CEO Duality

CEO Duality refers to the situation where the CEO also holds the position of chairman of the board. This situation is often referred to as the United States (US) model, and has evidence both supporting and rejecting its value.

The industry leaders were unanimous in their rejection of this option as it is an imperfect structure (Juliet Mclean) which lacked accountability (Henry van der Heyden). Without a clear separation between management and governance, or the CEO and the board, the lines easily blur and you are missing what governance is about (Colin Armer).

5.5.4 Revolving Chair

Section 2.7.1 the Board as a Team, explains how a board must work effectively together to add value. The majority of the industry leaders object to the idea of a revolving chair. They believe that the chair requires a specific skill set, and that not every individual has these skills. Therefore by selecting the right person to be the chair, the chair could lead the board into robust and value-adding conversations and decisions. This point was noted by Chris Kelly, Colin Armer, David Graham, Henry van der Heyden and John Wilson in section 4.4.6. All the above agreed that a specific skill set is needed. In addition, Colin Armer also alluded to the need for stability so that a relationship can develop between the CEO and the Chairman.
The only industry leader who identifies a use for a revolving chair is Mark Townshend. He believes that in the right situation a revolving chair can be used as a personal development tool to teach individuals how to chair a meeting. He thinks that this would only work successfully if the board has someone who has experience to guide and nurture the process.

**5.5.5 Director Election**

The directors were unanimous in their approach to director election. Directors must be elected by the shareholders as this is their fundamental right under the farm constitution. However, associated and independent directors are normally selected by the board, and approved by the shareholders.

**5.5.6 Selection on Prestige**

Prestige is a the widespread respect and admiration felt for someone or something on the basis of a perception of their achievements or quality (Oxford Dictionaries, 2013). The industry leaders were asked if directors should be selected on their prestige. While they acknowledge that this happens, they suggest that it should not. Directors should be selected on their merit and capabilities. John Luxton pointed out that selection on prestige can be used to attract media attention but this can be a costly and an ineffective way to gather attention without adding value to the board, which in turn removes some of the advantages of governance.

**5.5.7 Director Personality Types**

The literature suggests that director personality types can have an effect on the level of efficiency at which the board operates. The industry leaders do not agree with this perspective, and suggest that **everyone adds value to the company in their different ways (Chris Kelly)**. Personality types do add some value as **you still need all the different personality (Barbara Kuriger) types to get a robust discussion**. Colin Armer suggests it is more important to focus on individual **integrity and principles** than personality types.

**5.5.8 Training for Directors**

While the literature suggests that formal training is important to be a successful director, the industry leaders disagree. Some industry leaders propose that formal training only accounts for 2% of what is required to be a good director. Instead some suggest that directors need to have industry experience and that they will be better well-rounded directors if they **have got out there and done the hard yards (John Wilson)**.

**5.5.9 Summary of Board Composition**

The industry leaders agree that the composition of a board is critical to getting the right combination of individuals to achieve a value-adding board. However, this should be achieved by getting the right
mix of individuals who have the skill sets that are required in order for the business to pursue its objectives. This includes the view that CEO duality is inappropriate. This approach allows the right mix of people to be on the board, rather than a token approach of selecting an individual from all categories and hoping to achieve diversity and in turn achieve a value-adding board.

5.6 Ownership Considerations

Dairy farm governance within New Zealand is both a diverse and complex issue. This stems from the nature of the New Zealand dairy industry, which operates in a dynamic and ever changing context, a context which allows astute businesses to capitalise on the opportunities available. Due to this, the New Zealand dairy industry ownership is no longer made up entirely of the typical husband and wife partnership but instead made up of an array of different structures. These different ownership structures heavily influence the operation of the business, and if not managed correctly can quickly become a weakness of the business. This is discussed below:

5.6.1 The Role of Boards in Family Firms

Many small firms are family owned. This is often the case within the New Zealand dairy industry (Cooney, 2012; van Bysterveldt, 2012). Bertrand and Schoar (2006, p. 74) suggest that family firms are commonly “characterized by a concentration of ownership, control and often key management positions among family members, even after the retirement of the firm’s founders”. Bammens, et al. (2008) suggest that a family firm needs controls to be centred around three areas: task conflict, family experience and intentional trust.

The industry leaders speak indirectly of these controls. They suggest that in a family situation, knowledge of these issues is more critical than ever before. This is because in a family situation, it’s ten times worse if it falls apart (Barbara Kuriger). The industry leaders suggest two actions to reduce the chance of adverse actions. Firstly, they suggest that there should be a higher percentage of independents on the board as they don’t have the emotional connection influencing their decisions. Secondly, they suggest that there is a pre-established criteria that must be met before any family member can be involved within the business.

5.6.2 The Role of Boards in Small to Medium Enterprises (SME)

New Zealand dairy farming businesses fall under the New Zealand definition of small to medium enterprises, which adds a different aspect to governance. All of the industry leaders suggest that there is very little difference in the principles used to govern a SME compared to their larger counterparts, as the only real difference may be the complexity of the issues at hand.

The literature suggests that in smaller businesses, managers will predominately have the majority ownership share within the enterprise (Huse, 1990). The literature suggests that this could make the
rest of the owners ‘merely subservient’ (Mace, 1971, p. 87), as they will be unable to prevent them from acting upon their positions of power. The industry leaders suggest that by establishing a board, the directors are legally bound to look out for the best interests of the company (Henry van der Heyden).

The industry leaders further suggest that while issues faced by SMEs may be less complex compared to that of their larger counterparts, they often have less internal competency to deal with these issues. This is because SME boards do not have internal sources for service, expertise and control (Huse, 1990). It is for this reason that the industry leaders reiterate the importance of independent directors. This is because independent directors bring in a specialised skill set to help guide the business in the direction that it is pursuing. As this pursued direction changes, Juliet Mclean and John Luxton suggest that the independent directors should also change, or that another independent director with the required skills should be added.

5.6.3 The Role the Board Plays Regarding Institutional Arrangements

The literature discusses the term ‘institutional arrangements’. While governance and ‘institutional arrangements’ often interrelate there is a separation between the two (Rosairo, 2010). Institutional arrangements usually refers to the rules adopted by enterprises to facilitate coordination and govern relationships between stakeholders, within and outside the enterprise. Many of these institutional arrangements are formally defined by the enterprise’s own constitution and by legislation that applies to their choice of business structure. Institutional arrangements is the area that the industry leaders suggest has the biggest impact on the style of governance that is used for an enterprise. There is different legislation defining each ownership structure, therefore the governance used within these individual structures must be relevant. It is for this reason that the industry leaders suggest that this aspect of the business should be decided with due care and with the consultation of expertise (Barbara Kuriger).

5.6.4 Summary of Ownership Considerations

This section discussed the impact of different ownership considerations that are relevant to the New Zealand dairy industry. As shown, this does not alter the fundamental principles of governance. However it does introduce different factors for consideration. These unique factors of dairy family farms need to be acknowledged by the board of directors if the board is to protect the company and add value.

5.7 Board Dynamics

Board dynamics are less to do with formal structures and more to do with the quality of the directors themselves and how they interact (Nadler, 2004). Results from the research suggest the following
aspects of board dynamics are important, including the boards interaction as a team, a board operating model, reporting and the use of an advisory board.

5.7.1 The Board as a Team

Past research neglects the human side of corporate governance (Huse, 2007), due to this the board is rarely seen as a team. Together they are governing the enterprise towards a common goal of greater success. The industry leaders are largely in support of this concept. This is because the combined skills of a group working towards a common goal are superior to that of an individual. Therefore, if the dynamics of a board function effectively as a social unit and if the board is able to build good relationships with management including a high level of social dynamics, the enterprise can become more constructive in its governance methods, leading to successful day to day management system (Huse, 2007; Nadler, 2004).

The industry leaders suggest that personality types add to the functionality of the board, helping the board to operate as an effective team. Contrary to the literature, the industry leaders suggest that there are very few negative personality types. This is because their experiences suggest that a variety of personality types allows discussion to be seen from different viewpoints (Chris Kelly).

5.7.2 Board Operating Models

The continuum set out in section 2.7.2 is a model of where boards operate. A board will move along this continuum at different points in its lifecycle (Nadler, 2004). The industry leaders agree with this to a point. While they see the need for an operating board in times of crisis, they cannot see the time when a passive board would be suitable. This is because a passive board would not be operating under good governance principles and legally you can’t have limited accountability as a director (Henry van der Heyden). Every industry leader suggests that a good board should sit in the middle of the scale and operate as an engaged board, as this is what a board is for: to engage and help the CEO (Chris Kelly). Thus, it is advantageous to the enterprise to observe where along the continuum their board sits and make the relevant changes so the board and the enterprise can become more productive and effective. Table 5-1 below identifies where the industry leaders feel a board should sit on the continuum. If the industry leader identifies positively with a model it is highlighted in Green. Red boxes show a strong negative reaction to this model. Orange boxes suggest that the industry leader identifies with this operating model at different points in the enterprise’s lifecycle.
Table 5-1 Board Operating Models

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<th>The Passive Board.</th>
<th>The Certifying Management Board.</th>
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<td>J.van der Poel</td>
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<td>M.Townshend</td>
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<td>J.Wilson</td>
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5.7.3 Reporting to the Board

The industry leaders suggested that information is fundamental for the enterprise to become competitive and profitable in the short term and successful in the long term. Therefore boards require timely information for making decisions. A structure is recommended to ensure that the management team knows what information is required and when it is needed.

5.7.4 Advisory Boards

The literature on advisory boards suggests that this is an effective middle ground for governance. However, many of the industry leaders do not agree with this as they believe it lacked teeth (Henry van der Heyden) referring to its lack of accountability. The industry leaders suggest that this is not the way for the industry to move forward as this is more of a management tool than a governance tool.

5.8 Specific Research Questions

The literature review determined a gap in the literature: What are the governance needs for New Zealand dairy farming enterprises? Specific research questions were developed to attempt to answer this overarching question. The questions are answered below:

1. What role should governance play within New Zealand dairy entities according to dairy industry leaders?

This study suggests that governance is applicable to all New Zealand dairy farming enterprises. However it is important to understand that every dairy farming business is unique, and will require a
different level of governance. If this is not achieved, then any benefits will be outweighed by the financial cost of applying an incorrect level of governance to the enterprise. As farming businesses become more complicated, the need for governance will increase.

2. What is the underpinning role of the board for dairy farming enterprises?

This study suggests that the underpinning role of the board in dairy farming governance, is an increased need for “control”. This is a unique finding in governance research on dairy farming enterprises. The board must have the ability to deal with this role, which may stem from the separation between the enterprise’s owners and the enterprise’s operators. This separation means that the owners lose the ability to control the operation of the business on a daily basis. The operators (farm managers) are immersed in the business as they both live and work on site. This means they are in a position to take advantage of situations for their own benefit. The board is tasked to observe and control this self-prevalent behaviour so that the enterprise is aligned with the objectives of the owners.

3. What part does board composition play in dairy farm governance?

Composition is a vital component for achieving a board that is able to function at a level where it adds value to the enterprise. This study finds that while most individuals will add value at some level, a good board will be made up of carefully selected individuals. This is because it is important to ensure that all the directors have the required skill set to support the enterprise. Within a dairying context, independent directors are considered necessary by the industry leaders as they are unbiased in their opinions and offer different skill sets. However, independent directors are the only director types mentioned in the above literature review to be singled out by the industry leaders. The industry leaders suggest that selecting directors based on their personal attributes such as being female may be counterproductive. A director should be selected based on their skill set and capabilities alone.

4. What part do board dynamics play in dairy farm governance?

A board must be aware of the dynamics that affect their actions. What distinguishes a good board is their ability to work as a robust and effective social system. Selection of functional personality types will add value, whereas dysfunctional personality types will hinder a board’s working relationships. It is important that a board understands this; otherwise, they are just a group of individuals rather than a team made up of individuals working with a common purpose. If a board becomes a group of fragmented individuals, rather than a team, it will be hard for the board to respond to change. If a board is in control of its operating model, then it can react as required which increases their efficiency and productivity.

5. What part does board reporting play in dairy farm governance?

Reporting is of utmost importance to the board. The board requires timely and relevant information in order to make an informed decision. This needs to be presented to each individual prior to a meeting to
allow time for review and analysis. This is important for the enterprise as it will allow robust discussions that lead to the best direction for the enterprise.

6. What effect do processes have on dairy farm governance?

There are underlying processes that are best practice for a board. This study has found that governance should always be a formal process. The dairy industry should not allow the standard of governance to become casual or relaxed, as this would reduce accountability, which is an important aspect of governance. Thus, meetings should be conducted in a formal setting and include all the processes that add rigour e.g. appropriate board minutes

7. Do industry leaders consider the role of dairy farming boards to be different compared to other organisations?

The industry leaders suggest that there is no difference in the way they govern a dairy farming enterprise compared to other industry organisations in which they are involved. This is because the fundamental principles of governance, and what governance is designed to achieve, remain the same regardless of the context to which governance is applied. However, they suggest the role of control and the enterprises ownership and operational considerations are more important in the context of a dairy farming enterprise.

8. Do boards of directors add value/create additional value for dairy farming enterprises?

This study suggests that governance will add both financial value and create additional opportunities for the business if it is applied correctly. Financial value will come from two avenues. Firstly, the board will hold the enterprise accountable, thus giving them the ability to review spending, make adjustments and provide counsel so that the best investment decisions are made. Secondly, it has been identified that the rigour provided by a board means that financial institutions will look favourably upon a business. Non-financial value is also added as a board brings in diversity of thought which will bring in new ideas and opportunities for the enterprise to consider.

5.9 Conclusion

Research on dairy farm governance, from the perspectives of the interviewed industry leaders has illustrated the need for governance. The interviews conducted indicate that dairy farm governance follows prescriptions in existing literature in many situations, but in some industry specific issues there are notable differences. This research suggests the type of governance adopted by a dairy farming enterprise is largely driven by the ownership and operational structure.

This research has found that there is no one governance theory that can be generalised to the dairy farming industry as a whole. Results from interviews with industry leaders indicate that two of the four theories identified have the most relevance; these being agency theory and stewardship theory. If
management are acting in the interests of those involved in the ownership structure, then stewardship
theory prescriptions are prevalent. However, if management are acting for their own benefit, then
agency theory outcomes are prevalent. Both outcomes have different implications for the board in its
governance of the firm. By understanding these theories and that dairy farming is a ‘personally
intensive’ business, due to the personal relationship farmers have with the land, a board may be able to
identify and act to make changes to ensure the enterprise is operating to its potential.

The three widely accepted roles of the board; strategy, control and service, are important within the
context of a dairy farming enterprise. As shown in Figure 5-1 these spheres overlap which indicates
these roles are interconnected. However, they are not equal size spheres. The board must understand
that in farming, control is considered the most important role. It is recognised that farmers have a
personal relationship with the land due to it often being their home, their livelihood and their
workplace. This increases the difficulty in separating ownership from board control. As control is
important, the motives of different managerial parties must be recognised. If the board is not able to
resolve these issues, it will have a negative effect on the other two board roles, because of their
interconnected relationships.

The findings on board composition is an important element to this study. The industry leaders suggest
that a board ‘must and must not’ contain certain people in order to create a functioning board. They
suggest that the selection of directors should depend on the individual’s capability. By focusing on
capability rather than token directors (e.g. woman, prestige, majority shareholders), the firm gathers a
group of individuals who have the correct skill set for adding value to the company. The objective of
separating governance and management means that CEO duality is not supported. CEO duality blurs
the line between governance and management. In addition, having a revolving chairman does not
recognise that the role requires an individual with a certain skill set. Not everyone will possess, nor
should you want them to possess, every necessary skill set if you are looking to achieve robust
discussion.

The dynamics of the board and how they interact is important. The board should work together with
the common goal of adding value to the enterprise. Therefore, in many respects they are a team. Their
ability to act as a team, although they may meet only a few times a year, is important. It is also
important for the board to realise its own dynamic in relation to its operating model. A board needs to
understand how they function to ensure they are adding value through governance. The industry
leaders recommend the engaged board method. In this model, the board serves as the CEO’s partner. It
provides insight, advice and support on key decisions. It recognises its responsibility for overseeing
the CEO and company performance. The board should conduct substantive discussions of key issues
and actively defines its boundaries. A number of specific recommendations were obtained. These
findings are listed in Table 5-2.
Table 5-2 Summary of Findings from this Study

<table>
<thead>
<tr>
<th>Findings Considered Important from this Study</th>
<th>Findings this Study Suggests should be Avoided</th>
</tr>
</thead>
<tbody>
<tr>
<td>Understand why the enterprise requires governance</td>
<td>CEO duality</td>
</tr>
<tr>
<td>The context of the enterprise is important for governance</td>
<td>Token directors</td>
</tr>
<tr>
<td>Control is the most important role of the board</td>
<td>Revolving chairman</td>
</tr>
<tr>
<td>Independent directors are important</td>
<td>Appointment on prestige</td>
</tr>
<tr>
<td>Governance should always be at a formal level</td>
<td>Dominance by majority shareholders</td>
</tr>
<tr>
<td>Separate management and governance</td>
<td>Passive boards</td>
</tr>
<tr>
<td>A board should be comprised of a wide selection of personalities</td>
<td>Amateur or inexperienced family members as directors</td>
</tr>
<tr>
<td>An engaged board is the suggested model</td>
<td>The manager should not be the board chairman</td>
</tr>
<tr>
<td>Boundaries of the board need to be well defined</td>
<td></td>
</tr>
<tr>
<td>Family board members should understand what is involved and what is expected</td>
<td></td>
</tr>
<tr>
<td>Directors should be selected on skills and experiences</td>
<td></td>
</tr>
<tr>
<td>The inclusion of majority shareholders should be case dependent</td>
<td></td>
</tr>
<tr>
<td>Shareholder agreements and exit strategies are important</td>
<td></td>
</tr>
<tr>
<td>Board decisions should be reached by consensus</td>
<td></td>
</tr>
<tr>
<td>The level of reporting is important</td>
<td></td>
</tr>
<tr>
<td>Consistent agendas are a good practice</td>
<td></td>
</tr>
</tbody>
</table>

5.10 Contribution to the Body of Knowledge

Traditionally, dairy farms have been operated as ‘husband and wife’ partnerships. Over the past two decades, dairy farms in New Zealand have increased in size and owning multiple farms has become more common. Consequently, increasingly complex business structures have developed. These developments have led to an increasing interest in governance. Although there is a wealth of information surrounding governance in other industries, this research has investigated the governance needs of a rapidly developing and evolving dairy industry in a small economy. Industry leaders have shared their experiences in governance of their own farms, and also their experiences from governance in a number of other off farm enterprises.
From the analysis of the interviews, it is proposed that although similarities exist between the SMEs that make up the New Zealand dairy industry and other industries, most New Zealand dairy industry SMEs operate under agency or stewardship theory prescriptions. It has also been established that in a situation where ‘your business is also often your home’, control rather than strategy or service is the most important activity of the board. Although the literature suggests a wide range of board operating models and composition, the research indicates that for dairy farming in New Zealand, an engaged board with a variety of personalities selected because they possess the appropriate skills, is desirable. The board needs to be operated in a formal manner, with well defined boundaries, and needs to avoid CEO duality. Figure 5.1 makes adjustments to previous theoretical models, most importantly suggests that those considering governance need to be aware of the need for these structures and the context within which their enterprise will operate.

5.11 Future Research

Due to the lack of governance research concerning New Zealand dairy farming, there is a wide array of potential research that could stem from this study. Future research suggestions include:

1) Use in depth case studies of specific dairy farming enterprises within New Zealand to further understand this research’s findings.
2) Survey a large group of farmers to determine if this study’s findings are applicable across the population.
3) Use selected individual case studies, to determine the areas from this research, that have been helpful to them in setting up governance structures for their enterprises.
4) Further explore the ownership and operational considerations element of this research in detail.
5) Explore board dynamics in the context of dairy farming.

5.12 Limitations of Research

This study is influenced by the limitations of qualitative research. Due to the researcher’s choice of case studies, it is more difficult to maintain, assess, and demonstrate rigour within the study. Also, due to the interviewing method of semi-structured interviews, the research quality is heavily dependent on the individual skills of the researcher and more easily influenced by the researcher's personal biases and idiosyncrasies. As the interviews are based in human conversations, the researcher's presence can affect the subject’s responses. This conversation method also adds to the volume of data gathered which makes analysis and interpretation time consuming. These factors were largely overcome by the chosen research method. This method utilised two dictaphones to ensure the accuracy of the data. NVivo was then used for in-depth cross-case comparisons of the transcripts.
Another limitation to this study is the researcher’s selection of industry leaders. While the eleven people interviewed in this research are relevant to the study, they are not the only candidates whose views could have been considered.
REFERENCES


SPARC. (2009). *Nine steps to effective governance: Building high performance organisations*: SPARC.


A. Opening Letter to Industry Leaders

Dear (name of participant)

I am a Masters student in the Department of Agricultural Management and Property at Lincoln University. I would like to invite you to participate in the research I am undertaking as part of my studies. This research has been approved by the Lincoln University ethics committee and funded by the Centre of Excellence in Farm Business Management. My research project, titled ‘Dairy Farm Governance: The Perspective of Industry Leaders within the Dairy Sector’ sets out to examine the following problem statement;

What are the governance needs for New Zealand dairy farming firms?

As the title suggests, this research will look at the current needs for governance through the eyes of ten selected industry leaders. The need for this research is inspired by the changing nature of the structures and operations of dairy farm ownership in New Zealand. These enterprises are substantial businesses in terms of assets, turnover and numbers of staff employed. Given these trends, an understanding of the governance of large dairy businesses will be increasingly important to the New Zealand dairy industry.

Your participation will involve an interview which should last no more than one hour. This interview will cover central issues such as strategic direction, composition and the associated board dynamics. I can undertake the interview at a time and place that is convenient for you. I would want to record and transcribe the interview. All interview data will be confidential and will be stored securely. However information about the project, including interview data, will be shared with my supervisors and other appropriate staff at the university.

I appreciate you giving time to this study and if you have any questions please do contact me at 0273238280 or alice.sterritt@lincolnuni.ac.nz. Or you can contact my supervisors Dr Kevin Old at 033253810 extn 7810 or kevin.old@lincoln.ac.nz or Dr Marvin Pangborn at 033218363 or marvin.pangborn@lincoln.ac.nz.

Yours sincerely,

Alice Sterritt
B. Information Sheet

Information Sheet for Participants

1. Title of Project:

Dairy Farm Governance: The Perspective of the Industry Leaders within the Dairy Sector

2. Researchers Name and Contact Information:

Alice Sterritt
91 State Highway 30, R.D.1 ATIAMURI.
Ph. (027) 3238280
Email: alice.sterritt@lincolnuni.ac.nz

3. Supervisor’s Name and Contact Details:

Dr Kevin Old
Ph. (03) 3253810 extn 7810
Email: kevin.old@lincoln.ac.nz

Dr Marvin Pangborn
Ph. (03) 3218363
Email: marvin.pangborn@lincoln.ac.nz

Brief outline of the Project:
This project will investigate and document the current and recommended role for dairy farm governance within the New Zealand Dairy Industry.

4. Company or Origination Sponsoring or Funding the Research:

The organisation funding this research is the ‘Centre of Excellence in Farm Business Management’.

5. Explain how any publications and/or reports will have the consent of participants, and referenced correctly:

Prior to each interview each participant will be asked to read and sign a consent form for participants. This form encourages you (as a participant) to receive satisfactory replies to any questions regarding the study and highlights your ability to withdraw from the research at any time. Post interview you will receive a transcript of the interview to ensure you are happy with your recorded dialect. This will allow you to make any changes or alterations.

6. How will your Process Allow People to:

A) Refuse to answer any particular question and withdraw at any time.
As a participant you will be asked to sign, prior to the interview, a consent form outlining that you may refuse to answer any question(s) and may withdraw from the study at any time.

B) Ask any further questions about the study, which occur during participation.
You will be asked to read this participation information sheet encouraging you to ask any questions you may have about the study. This will also be highlighted orally at the beginning and end of the interviews.

C) Be given access to a summary of the findings from the study when it is concluded.
As an interviewee you will be provided with a copy of your interview transcripts and be invited to comment on them. A summary of findings will be made available to participants at the conclusion of the study.

7. Explain what will happen to the information collected from participants?

The data collected from the participants will be analysed and will contribute toward a Master’s thesis. Upon completion of this research the evidence collected in this research will be archived and may be used for further research.
C. Consent Form

LINCOLN UNIVERSITY
Department of Agricultural Management and Property

‘Dairy Farm Governance: The Perspective of Industry Leaders within the Dairy Sector’

Consent Form for Participants

I have read the Outline of Research Project form for this study and have had details of the study explained to me. My questions about the study have been answered to my satisfaction, and I understand that I may ask further questions at any time.

I also understand that I am free to withdraw from the study at any time, or to decline to answer any particular questions in the study. I agree to provide information to the researchers under the conditions set out on the Information Sheet.

I agree to participate in this study under the conditions set out in the Outline of Research Project form.

Signed: ________________________________

Name: ________________________________

Date: ________________________________

Researcher’s name and contact information:
Alice Sterritt
91 State Highway 30, R.D.1 ATIAMURI.
Ph. (027) 3238280
Email: alice.sterritt@lincolnuni.ac.nz

Supervisors Name and Contact Details:
Dr Kevin Old
Ph. (03) 3253810 extn 7810
Email: kevin.old@lincoln.ac.nz

Dr Marvin Pangborn
Ph. (03) 3218363
Email: marvin.pangborn@lincoln.ac.nz
D. Interview Guide

Interview Guide

Designed for the Industry Leaders within the Field of Dairy Farm Governance

1) How did you enter the dairy industry?
Prompt to get full story… (Beginning, middle, end)
Are all interests in New Zealand?
What are the farms locations e.g. km apart and location?
What is the business structure of your farms?

2) Can you please tell me about your off farm governance roles?
Prompt to get full story up (Beginning, middle, end)
Why did you get into this?

3) How have you established governance on your farm?
Prompt Questions:
How did you do this?
Why did you do this?
If you could turn back the clock would you do it different?
Do you think the creation of a board has added value? How? Why?
In your opinion what are the 4 or 5 ‘must do’s’ when setting up a dairy farming
board?

4) How do the off farm governance roles differ to the governance you currently use for
your dairy farm interests?
Prompt Questions:
In your opinion what are the 4 or 5 major differences between the two roles?
What knowledge have you taken from your off farm roles and utilised on your dairy
farming board?
How much time is involved in a dairy farming board?
Do family dynamics complicate dairy farming boards?
Does the SME size of most dairy farms reduce the need for dairy farming boards?

5) In your opinion, how should a dairy farming board be structured?
Prompt Questions:
Are Directors selected on personal attributes?
Do you think female directors add value? (how many are on your board)
Do you use Independent directors? Why/why-not?
Should majority shareholder automatically get on the board?
What do you think is the ideal number of people on a dairy farming board?
Is the CEO and the chairman normally the same person?
Who should chair the board? Is a revolving chair better?
Who elects directors?
In your experience do certain personality types add or detract value?
Do you select directors on their individual prestige to add to the reputation of the
board?

6) Do you hold formal board meetings for you dairy farming enterprise?
Prompt Questions:
When and where are these held? E.g. Farm ute on tour round farms?
How often are meetings held?
What is required of an individual for preparation for the meeting?
What are the 4 or 5 biggest topics of discussion?

7) In your experience, how do directors develop strategy and vision for the business?
Prompt Questions:
- How is this process monitored?
- How often do you review this strategy?
- How do you maintain control of this strategy with managers having day to day control of the farm?
- What reporting do you expect from managers?
- How do you monitor management? Closely/loosely?
- Do advisory boards help this process of setting strategy?
- Did the GFC affect your governance model?

8) Does the dairy farming board set the constitution of the enterprise?
Prompt Questions:
- Do they set the exit strategy?
- Do they set the entry requirements?
- How do they handle the entry/exit of capital?
- Can a shareholder leave as they please?

9) What is the most important role (as you see it) of a board of directors on a dairy farm?
Prompt Questions:
- Why did you suggest those roles over others?

10) What do you think are the biggest challenges dairy farms boards will face in the future?
11) Where would you suggest that dairy farming board should sit along this continuum to be most effective?

The Passive Board. This is the traditional model. The board's activity and participation is minimal and at the CEO's discretion. The board has limited accountability. Its main job is ratifying management decisions.

The Certifying Management Board. This model emphasises the credibility to shareholders and the importance of outside directors. The board certifies that the business is managed properly and that the CEO meets the board's requirements. It also oversees an orderly succession process.

The Engaged Board. In this model, the board serves as the CEO's partner. It provides insight, advice and support on key decisions. It recognises its responsibility for overseeing the CEO and company performance. The board conducts substantive discussions of key issues and actively defines its boundaries.

The Intervening Board. This model is common in a crisis. The board becomes deeply involved in making key decisions about the company and holds frequent intense meetings.

The Operating Board. This is the deepest level of on-going board involvement. The board makes the key decisions that management then implement. This model is common in early stage start-ups where top executives may have specialised expertise but lack broad management experience.

12) Is there anything else you would like to add to this interview on dairy farming governance?