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## RETHINKING BOARD ROLE PERFORMANCE: TOWARDS AN INTEGRATIVE MODEL

**ABSTRACT:** *This research focuses on the board role evolution analysis which took place simultaneously with the development of different corporate governance theories and perspectives. The purpose of this paper is to provide understanding of key factors that make a board effective in the performance of its role. We argue that analysis of board role performance should incorporate both structural and process*

*variables. This paper's contribution is the development of an integrative model that aims to establish the relationship between the board structure and processes on the one hand, and board role performance on the other.*

**KEY WORDS:** *corporate governance; board of directors; board roles; board effectiveness*

**JEL CLASSIFICATION:** M10, G34, M14

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## 1. INTRODUCTION

The corporate governance field generally distinguishes between internal and external corporate governance mechanisms. Internal mechanisms include the ownership structure and the boards of directors<sup>1</sup>, whereas external mechanisms correspond to corporate market control and the regulatory system.

The boards as an internal mechanism of corporate governance represent “the link between individuals that provide the capital (owners) and individuals exploiting that capital in order to create value (managers). This implies that the boards connect a small, powerful group that leads a company, and a large, diffuse, and relatively powerless group simply wanting the company to be well led” (Monks & Minow, 2002, p.164).

Board effectiveness is seen as the degree to which boards are successful in carrying out their roles. Much of the extant corporate governance literature recognizes different board roles: monitoring role (Fama, 1980; Zahra & Pearce, 1989), control role (Zahra & Pearce, 1989; Baysinger & Hoskisson, 1990; Monks & Minow, 2002), and service role in corporate strategy development (Judge & Zeithamal, 1992; Pettigrew & McNulty, 1995), while Pfeffer & Salancik isolate the board role of facilitating the acquisition of critical company resources (Davis & Cobb, 2009).

This research paper focuses on the evolution of board roles which took place in parallel with the development of different corporate governance theories and perspectives. Mace (1971) argued that a board has passive and ceremonial roles (Pugliese et al., 2009), but ever since the understanding of board roles has evolved, in common with the traditional corporate governance perspective, to an active one that points to boards’ strategic role, addressed within a contemporary research perspective (Ingley & Walt, 2004; Kim, Burns, & Prescott, 2009).

The main research question we pose in this study is why there is a gap between what is, in theory, defined as board role expectations, and board role performance. In addressing this concern we analyze the factors influencing the implementation of different board roles. We then address key factors affecting board effectiveness: board structure and board process.

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<sup>1</sup> In this paper the term *board* will be used to denote *board of directors*, common in corporate governance research and literature.

Traditional research finds the structural factors, e.g., composition, leadership structure, and board size, to be the most relevant influences on board effectiveness. Alternatively, behavioural approaches emphasize as the key factors of board effectiveness those influencing the processes within boards, i.e., effort norms, cognitive conflict, and usage of knowledge, as well as board members' characteristics, including background diversity and behavioural characteristics. Factor analysis indicates that a new integrative framework for board effectiveness evaluation is much needed as a good starting point model for further empirical research. It is also suggested that the proper model implementation is contingent on its adjustment to the given socio-economic circumstances.

## **2. BOARD ROLES**

Board roles have been the focus of numerous authors' research since the 1980s (e.g., Donaldson & Davis, 1991; Weir, Laing, & McKnight, 2002; Denis & McConnell, 2003; Babić, 2010). Under conditions of separate ownership and control, owners' and managers' interests may differ; which is why the essential issue is how to ensure that managers perform in the interest of owners. In finding a solution traditional research kicks off with the core agency theory hypothesis, that managers as stakeholders' agents, that is principals agents, may make decisions contrary to the owners' interests. In the other words, there is need to monitor managers to ensure that their decisions focus on protection of stockholder's wealth (Halme & Huse, 1997).

From the agency theory perspective, the board as an internal governing mechanism has the authority to control the work of agents through ratification and monitoring during the decision-making process (Fama & Jensen, 1983). Accordingly, Fama and Jensen (1983) isolated decision control as the basic board role, which later was thoroughly analyzed in the work of Baysinger and Hoskisson (1990) by establishing two decision control types – financial and strategic control. Financial control leads to short-term profit maximisation and is based on evaluation of managers' performance, whereas strategic control addresses a company's long-term existence and profitability. Fama and Jensen (1983) argued that the board's role of decision control combined the phases of ratification and monitoring in the decision-making process. According to Zahra and Pearce (1989) the focal board roles include the control role, the service role, and the strategic role. These classifications are complementary, and therefore may be related.

The control role refers to performance evaluation of top management, and is related to decision control activities. It concerns top managers' recruitment, dismissal, and evaluation, or in other words, monitoring, control, and review of managers' work performance so as to protect the owners' interests. The control role also involves board members' responsibility for CEO election, monitoring of their work, report audits, and ratification of decisions (Zahra & Pearce, 1989). Reactive in nature, the control role implies an ex-post analysis of managerial behaviour. Subsequently, the board assumes the tasks and responsibilities as follows: selection and election of the CEO, promotions and dismissals, monitoring and company's performance evaluation, ratification of important decisions, and reduction of agency costs (Levrau & Van den Berghe, 2007a).

Following the development of resource dependence theory and stewardship theory, understanding of board roles and responsibilities altered. The resource dependence theory comprehends the board as a mechanism for co-opting important external organizations with which the company is interdependent. One of the possible strategies is to appoint representatives of competitors, key suppliers, or customers to the board. According to Pfeffer and Salancik (1978) board members provide advice and expertise, access to resources, and legitimacy, and also contribute to strategic decision-making by providing access to key resources (Davis & Cobb, 2009; Pugliese et al., 2009; Hillman and Dalziel, 2003). This implies that the board has a service role related to management decision-making activities: co-opting external influences, realizing contacts between board members and relevant individuals to ensure pivotal company resources, ceremonial activities, and enhancement of the company's reputation, and advising the management during the strategic decision-making process. While the management bears the responsibility for the development of new strategy, the boards' advisory role in fact enables their indirect influence over the strategic decision-making process (Nicholson & Newton, 2010).

Conversely, the stewardship theory pioneers strategic engagement as the core board role, excluding both legitimacy and resource dependence concepts (Levrau & Van den Berghe, 2007a). This theory argues that the interests of managers and board members are not necessarily in conflict (Pugliese et al., 2009). In this context, Huse (2007, p.54) argues that "the core concept of stewardship theory is trust between managers and owner". Contrary to the agency theory based on the hypothesis of managerial opportunism and the need for strengthening the board control role, the stewardship theory is build on the fundamental concept that managers act as good stewards in the corporation's interest (Davis et al., 1997). The level of accomplished performance is determined by the capability of the CEO to

design the structure of the organization in accordance with the demands of the situation and strategic activities of the corporation. The successful formulation and implementation of the strategy depends on clearly defined roles and the shared authority and responsibility of the managerial structure on the corporate, business, and operating levels (Babić, 2010). In this view the primary board role is to support and assist managers in reaching the company's objectives, and not to control them. Put differently, the stewardship theory suggests that the board's main role is in fact to guide management towards achieving the corporation's mission and objectives (Huse, 2007, p.55).

The board's roles may also be explained via two different perspectives - an active one and a passive one (Levrau & Van den Berghe, 2007a). According to the passive perspective, the board has no significant influence over the company's strategic development, and its responsibility is merely defined within the evaluation domain of the strategy adopted by top management. Mace (1971) argues that this concept may theoretically be clarified within the constraints of the managerial hegemony theory that gives the board the so-called rubber-stamp function, referring to strategy review and ratification role only, whereas the strategy itself is solely the responsibility of top management (Pugliese et al. 2009).

Strategic board role analysis by and large focuses on strategy review and ratification process, since boards are assumed not to be actively included in the process of strategy formulation and implementation. In contrast, according to the active perspective, boards are important strategic governing mechanisms, with a rightful role in the company's strategic development. The boards should thus actively participate in the strategic decision-making process and be involved in all its phases (Pettigrew & McNulty, 1995). The board members' experience deriving from their managerial positions in other corporations makes them competent for strategic decision-making and increases the level of boards' involvement in the strategic decision-making process. In this context, "boards are legally responsible for the strategy and they are in an excellent position to contribute to strategy" (Pugliese et al., 2009). Moreover, rapidly increasing stakeholder activism puts pressure on them to deal with strategic issues.

In line with the active perspective, development of the board's strategic role has been founded in the stakeholder theory. The key idea behind this theoretical framework is that good relations formed with strategic stakeholders are far more important than the notion of control. Hence, the managers' task is to formulate and implement processes through which the interests of both owners and different stakeholders (e.g., employees, consumers, suppliers, local community, financial

institutions, and other interest groups) will be satisfied and the company's long-term sustainable development accomplished (Babic, 2010). Due in large measure to the need for supporting stakeholders' interests, the board members have to assist top management in corporate strategy development. The stakeholder theory sets forth the strategic board role that addresses board activities related to defining corporate vision and mission, and concerning formulation, analysis, and ratification of corporate strategy. In this way the board's role is linked to both decision-making control and management, and thus refers to balancing and managing stakeholders' interests (Huse, 2007, p.53).

In accordance with the traditional research framework, the analysis of the board's strategic role is mainly centred on strategy review and ratification processes, given the hypothesis that boards have no active involvement in strategy formulation. However, a bulk of empirical research reveals the opposite; that boards are in fact included in the decision-making process relevant to strategy development and its implementation (Stiles, 2001).

The evolution of the board's role - from control to strategy (see Table 1) has been taking place in parallel with the development of different corporate governance theories, as follows:

- In line with agency theory, the main role of the board is controlling the managers and protecting the owners' interests.
- Resource dependence theory and stewardship theory concentrate on the board's service role of advising managers.
- Managerial hegemony theory explains the board's passive strategic role in strategy review and ratification functions.
- Stakeholder theory argues that the board has an active strategic role in the company's development with a high degree of involvement in the strategic decision-making process.

**Table 1.** Corporate governance theories and board roles

THE ROLES OF BOARD		
CONTROL ROLE	SERVICE ROLE	STRATEGIC ROLE
<ul style="list-style-type: none"> <li>• Maximize owners' wealth</li> <li>• The board monitors managers' activities to ensure that they are acting in the interest of owners</li> <li>• Selection and election of CEO, promotion and dismissal</li> <li>• Monitoring and evaluation of company's performance</li> <li>• Ratification of major decisions</li> <li>• Reduction of agencies' costs</li> </ul>	<ul style="list-style-type: none"> <li>• Board represents a co-opting external influence mechanism</li> <li>• Giving advice and supporting the management</li> <li>• Company representation</li> <li>• Ensuring critical resources</li> <li>• Guiding managers to accomplish company's objectives</li> <li>• Participation in strategy formulation and implementation</li> </ul>	<ul style="list-style-type: none"> <li>• Board has no significant influence over company's strategic development</li> <li>• The strategy is the province of top management – the board only plays review and ratification roles - passive perspective</li> <li>• Board is an important strategic mechanism in governing the company</li> <li>• Strategic decision-making: the board and top management are strategic partners in the strategic decision-making process - active perspective</li> </ul>
<b>AGENCY THEORY</b>	<b>RESOURCE DEPENDENCE THEORY</b>  <b>STEWARDSHIP THEORY</b>	<b>MANAGERIAL HEGEMONY THEORY</b>  <b>STAKEHOLDER THEORY</b>
THE THEORIES OF CORPORATE GOVERNANCE		

Source: adapted from Levrau, A. & Van den Berghe, L., 2007, p. 40 (Appendix 2).

### 3. RETHINKING THE BOARD'S ROLE

In line with the reasoning that regards boards as strategic management partners, the latest corporate governance research has been directed towards the board's role in creating corporate value. Given the increase in the number of requirements companies must fulfil towards different stakeholders and the general public, the creation of value does not merely imply creation of economic value, but rather addresses a wider set of parameters influencing the creation of social value.

Social value creation refers to employees' safety, ethical behaviour, programmes for employee training, corporate social responsibility, product quality, consumer satisfaction, environmental protection, etc. Creation of value does not only mean its distribution to the owners but a corporation's commitment to society, and thus the board's role should not be seen only as protecting the owners' interests (Huse, 2007, pp. 272-278). This standpoint indicates that corporate governance is increasingly seen as an instrument for balancing the interests of corporate stakeholders considered of vital importance for the continued existence of the corporation, and is less understood as a mere instrument for maximizing shareholder value (Dankova, 2006).

The development of the contemporary perspective on corporate governance is based on disputing the agency model (Huse, 2009b; McDonald & Westphal, 2010; Lan & Heracleous, 2010). Contrary to agency theory and the domination of the board's control role, the contemporary perspective is founded on the legal standpoint of the corporation as a principal that is consistent with stakeholder and stewardship theories. Rather than regarding the board as a mechanism acting in the owners' best interests and resolving conflicts between managers as agents and owners as principals, the contemporary perspective does not grant the owners the status of corporation principals, and managers are only perceived as one of the relevant stakeholders acting in favour of the corporation. The corporation holds the principal role and the board's main role is to mediate, i.e., the board acts as a mediator between corporation and stakeholders, aiming to balance the stakeholders' different interests. Board effectiveness is contingent on (a) the board's independence both in relation to the owners and with reference to all the relevant stakeholders, and (b) a defined system of priorities for decision-making (Lan & Heracleous, 2010), in accordance with the following three criteria:

1. Liability towards creditors, and not owners, except when the corporation is insolvent; in which case the fiduciary board's duties favouring creditors over owners may be abolished.
2. Satisfactory outcomes for all stakeholders, exclusive of favouring the interests of some.
3. The third issue refers to prioritizing interests if they collide. Addressing this concern depends on the stakeholders' power structure: the most powerful stakeholders prevail in conflict resolution.

In line with the above, a new approach to board role studies has been shaped, in the form of the director primacy model whose focal hypothesis redefines the board's role and status with reference to the owner-board-manager relationship.

The director primacy model relies on the stewardship theory which leans towards reliability, personal motivation, the need for self-actualization, collective orientation, and self-control of board members (Davis et al., 1997). This implies that board members should not be elected solely on the grounds of structural criteria and the often contested interpretation of the issue of board members' independence, given the ambiguity of the very term 'independence'.

The board is in charge, with the authority and responsibility to make decisions relevant to CEO election and dismissal, compensation, decisions on mergers and acquisitions, dividends, and the power to affect important elements of strategy. Even when the board does not take part in the strategic decision-making process, it holds the legal right to ratify decisions and evaluate if they are in the best interests of the corporation. The relation between board and corporation differs from the common agent-principal relation. The board members' power does not result from the agency relation with the owners, since the authority and responsibility of the board members are original and undelegated (Lan & Heracleous, 2010). The board members are to a great extent exempt from the owners' control, for they have a liability and obligation defined by law to act in the interests of the corporation as a whole. Hence, the board represents a key mechanism for decision-making, and owners are merely one of the relevant stakeholders. As a result the board controls the corporation's outputs and performs the role of mediating the hierarchy and balancing stakeholders' interests (Blair & Stout, 2001).

According to Blair and Stout (2001), the board members in a legal sense do not hold the role of agents, nor are they obligated to respond to the owners. Although the owners formally elect the board members, they need to be entitled and to have authority and responsibility to make decisions regardless of their ex-post evaluation. Given that the board members, in accordance with the law, can make decisions that put the owners' interests behind the interests of other stakeholders, it becomes obvious that board members in fact act as autonomous corporation fiduciaries<sup>2</sup> and do not perform the role of agents, as suggested by the director primacy model. Nevertheless, the director primacy model hitherto has not been implemented as the starting point in empirical research, and the redefining of key

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2 Corporate law stipulates that a fiduciary individual is somebody whom has been granted the power to act in the name and for the benefit of somebody else. The term fiduciary originates from latin word *fiducia* meaning trust, and thus a fiduciary is expected to act in the best interests of the beneficiary and have the sole objective of realizing of beneficiary's interests, even when the beneficiary, or in this case the corporation, cannot control the fiduciary's behaviour.

agency theory aspects (such as empirical dogmatism) remains the great challenge for numerous researchers in the area of corporate governance.

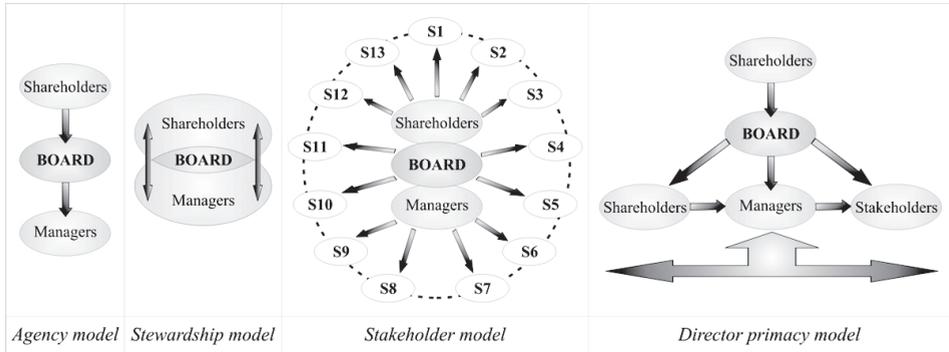
Figure 1 illustrates the evolution of board roles and models. In line with the traditional agency model, conflict of interests exists between owners and managers, and the board's role is to monitor and control managers (agents), ensuring they act in the interest of owners (principals). Boards therefore have the role of shareholders' fiduciaries (Castro et al., 2009). The development of the stewardship model changes the perception of the board's role. Here the starting hypothesis is that between the owners and managers there is no conflict of interests, so the board's role is to support managers who act as good stewards. In this perspective, "managers act as stewards of organizational resources and work in a manner to maximize shareholder wealth, and boards should facilitate and empower managers in the area of strategy" (Kim et al., 2009). The boards participate in strategy formulation and implementation through advising managers. Consistent with the passive perspective arguments, the strategy is the responsibility of top management, whereas the board's role is to review and ratify it (Castro et al., 2009).

Nonetheless, the evolution of the board's roles indicates that, contrary to the understanding of the passive perspective, the responsibility for strategy formulation and implementation is in fact held by both top management and board. Considered as strategic partner to the company's management, the board actively participates in the company's strategic development, given that the strategy is being formulated by the partnership approach. This notion forms a foundation for the stakeholder model that underlines the importance of establishing good relations with the vital, strategic stakeholders. The board's role is not merely the protection of owners' interests, but rather the balancing of many possibly conflicting stakeholders' interests. Hence, the board's role is to monitor management in the best interests of shareholders and external stakeholders, such as customers, the media, and local community and authorities (Halme & Huse, 1997).

The orientation toward the requirements companies must fulfil, with reference to all the stakeholders and not just the owners, resulted in redefining the board role, status modification of the owner-board-manager relationship, and the development of the director primacy model. This model is built on the hypothesis that corporations, rather than owners, have the role of principals, and the boards, as mediators between the corporation on the one hand and owners, managers, and

stakeholders on the other, have the role of corporation autonomous fiduciaries representing the company's interests.

**Figure 1.** Evolution of board roles



**Source:** Authors' figures

## KEY FACTORS IN BOARD ROLE PERFORMANCE

Corporate governance literature associates board role performance with a multitude of theoretical approaches identifying several board roles. For instance, board effectiveness may well be defined through 'task' outcomes deriving from fulfilling a set of activities (Minichilli et al., 2009b). Diverging theoretical concepts conclude that board roles and their performance are determined by different factors (Johnson et. al., 1996).

In parallel with the development of board roles and their modification, depending on the given theoretical perspective, the understanding of the factors with a dominant influence on the performance of board roles has also been altered, as has board effectiveness. In dealing with the factors influencing board effectiveness, corporate governance literature distinguishes two main research perspectives, traditional and behavioural.

### 4.1. Traditional Perspective

The traditional approach is based on the hypothesis that board structure determines its effectiveness, which is why defining the actual board structure becomes crucial. The traditional perspective further argues that sole understanding of board structural variables is sufficient for defining the principle

of effective board performance. Board structure is evaluated on the basis of three structural variables: board composition, namely the number of its external, independent board members; leadership structure (duality in board chairperson and CEO positions); and board size.

### **Board structure as a key factor of board role performance**

*Board composition.* From the traditional research perspective board composition (the number of its external, independent board members) influences board effectiveness and the company's financial results (Zahra & Pearce, 1989; Daily & Dalton, 1994a,b; Dalton et al., 1998). The theoretical research framework consists of agency and stewardship theories. With reference to the main agency theory hypothesis, that between owner as principal and managers as agents a conflict of interest exists and the board as an internal mechanism has the task of monitoring managers, board effectiveness is contingent on its independence from management. This line of reasoning implies that boards should be composed of a large number of independent members. Johnson et al (1996) find boards composed of a large number of independent, non-executive directors more effective, due to their enhanced capacity for objective control of managers.

However, this view is at odds with the stewardship theory, which holds that managers act in the owners' interest, and boards are thus better off composed of a large number of internal, executive directors. Board effectiveness depends on its strategic role, which implicitly affirms the hypothesis that boards composed of a large number of internal executive directors are in fact more effective because they possess the required knowledge, skills, and information for making strategic decisions (Levrau & Van den Berghe, 2007b). The given instances of being at odds with each other indicate that correlation between board composition and effectiveness depends on the theoretical research framework and the role of the board whose effectiveness is being evaluated.

*Leadership structure.* Consistent with the agency theory, separation of board chairperson and chief executive officer (CEO) positions constitutes a necessary board effectiveness hypothesis. Stewardship theory, on the other hand, argues that this duality in positions of board chairperson and CEO has a positive implication for board effectiveness, because it enables the concentration of power and authority in one person whose objective is accomplishment of the company's interests (Donaldson & Davis, 1994). Rather there is a need to establish an organizational structure that facilitates and strengthens corporate governance, other than the one enabling facilitated monitoring and control over

managers, as suggested by the agency theory (Dalton et al., 1998). Given the different agency and stewardship theories hypotheses, duality in the positions of board chairperson/CEO, and establishing the correlation between the leadership structure and board effectiveness, have been the research focus of various authors during the 1990s.

*Board size.* The number of board members is an important structural variable influencing board effectiveness. The agency theory standpoint is that the number of board members is an indicator of CEO domination. The more board members, the less the degree of CEO domination, and the better the monitoring of management (Zahra & Pearce, 1989). Also, boards composed of a large number of members have enhanced capacity for co-opting external influences and gaining critical resources for the company's success (Johnson et al., 1996). Along the lines of the given hypotheses, it is possible to conclude a positive correlation between board size and board effectiveness in performing control and service roles. Board size may affect the strategic board role as well. Judge and Zeithalm (1992) argue that board size and degree of involvement in the strategic decision-making process are negatively correlated. Once the boards are too large, constructive debate and creative conflict among its members become limited. In addition, if the strategic changes in the company's development are analyzed, a negative correlation can be concluded between board size and degree of strategic changes (Levrau & van den Berghe, 2007b).

#### **4.2. Behavioural Perspective**

While traditional research finds the board structure to be the key board effectiveness factor, the development of the behavioural perspective indicates that the actual board structure, although necessary, is not the only condition for board effectiveness (Leblanc & Gillies, 2005, pp.138). Although relevant, the given structural variables are not sufficient for establishing the correlation between board role expectations and board role performance. In other words, the study of board effectiveness requires the 'black box' between the observable board structure and board effectiveness to be opened in order to generate significant insights into board processes and board member characteristics (Leblanc & Gillies, 2005, pp.140; Ees et al., 2008).

#### **Board processes as the key factor of board role performance**

Understanding board processes as the key factor of board effectiveness has its foundation in *A Behavioral Theory of the Firm*, developed by Cyert and

March (1963) with the aim “to open up the black box of the internal workings of organizations” and explain the way in which decisions are made (Ees et al., 2009). Huse (2009b) finds that behavioural corporate governance theory mainly relates to the study of interactions and behavioural processes. Behavioural theory conceptualizes a new, behavioural research into board effectiveness.

The first significant steps forward in the development of the board effectiveness behavioural perspective were introduced in the late 1990s, when numerous authors pointed out the importance of understanding internal board processes (Pettigrew, 1992; Pettigrew & McNulty, 1995; Forbes & Milliken, 1999; Daily et al., 2003; LeBlanc & Gillies, 2005, pp. 139-145; Huse, 2005; Ees et al., 2008; Huse, 2009a; Minichilli et al., 2009a,b). “Boards of directors are decision-making groups facing complex roles whose performance is largely cognitive in nature” (Forbes & Milliken, 1999). Board effectiveness is closely related to socio-psychological factors influencing the decision-making process.

Consistent with this research, many authors conclude that board role performance is influenced by the following board processes: cognitive conflict, efforts norms, and use of knowledge and skills (Forbes & Milliken, 1999; Huse, 2005; Zona et al, 2007; Ees et al., 2008).

Cognitive conflict addresses the degree of disagreement among board members. This discrepancy is related to the tasks to be fulfilled and is a result of the different ideas, opinions, and knowledge that the board members possess. Because of the complexity of issues on the table, the board members may have diverse opinions, or perceive a particular situation differently. Cognitive conflicts within boards entail the implementation of critical processes and interactions for enhancing board effectiveness. However, apart from the positive effects, cognitive conflict may bring about negative emotions that lessen the attraction among the group members (Forbes & Milliken, 1999; Zona et al, 2007; Ees et al., 2008; Minichilli et al., 2009a,b). As a process variable, cognitive conflict has a positive influence on the role of control performance and a negative one on the role of strategic performance. This is explained through correlation between cognitive conflict and group cohesion. High level of cognitive conflict leads to a lesser degree of group cohesion, and thereby has a negative effect on the role of strategic performance.

Effort norms are evaluated on the basis of board members’ degree of activity in performing defined roles. The level of effort that board members exercise depends on their beliefs and expectations of being properly rewarded for

accomplishments. High individual effort will increase board effectiveness as a group (Forbes & Milliken, 1999; Zona et al, 2007; Ees et al., 2008). In other words, effort norms indicate the level of effort necessary for board members to accomplish the set objectives. High individual effort as well as strong effort norms can be expected to enhance the performance of all board roles. Effort norms have positive implications for control and strategic board roles. Enhanced board members' efforts lead to improved quality of both strategic decision-making and control processes.

The use of the knowledge and skills refers to the ability to apply them in board performance. The use of knowledge and skills should be set apart from the concept of cognitive conflict. The former relates to the process by which members' contributions are coordinated, whereas the latter defines the content of board members' contributions (Forbes & Milliken, 1999). Board members have to build relations based on mutual understanding and respect, and have a propensity towards creating synergy effects in their knowledge application. By and large the use of knowledge is the main process variable enhancing all board role performance.

### **Board members' characteristics as a key factor in board role performance**

Opening the 'black box' of board behaviour and understanding board processes implies the involvement of board members' individual characteristics in board effectiveness analysis. The extant literature differentiates between two groups of individual characteristics: background diversity and board members' behavioural characteristics relevant to board role performance.

Board members' background diversity as a factor influencing group dynamics and team performance is researched in depth in the work of Milliken and Martins (1996). These authors point to the relevance of understanding the influence different personal characteristics of board members (i.e., professional education, knowledge, and skills) have on the performance of the board as a group. Furthermore, a number of personal demographic characteristics such as race, age, gender, nationality, education, and functional experience are also suggested as affecting board relationships, and subsequently board dynamics and effectiveness (Petrović, 2008). Numerous authors following the further development of the behavioural perspective have come to similar conclusions. According to Minichilli et al. (2009a), board members' background diversity, as a characteristic indicating the degree of difference in experience and competences among board members, influence the degree of a board's success

in role performance. Skills or knowledge-based diversity may well have a positive influence on the board group effectiveness due to possible increased creativity and innovation in problem solving. Nevertheless, it may also have negative consequences, as when board members cannot work together to resolve issues. Different effects of board diversity on board role performance show that between the given variables a positive or a negative correlation may be established depending on the type of board role (Minichilli et al., 2009b).

With reference to the behavioural perspective, board effectiveness is influenced by the board members' behavioural characteristics. Core behavioural characteristics laying the foundation for a particular pattern of member behaviour (LeBlanc & Gillies, 2005, pp. 162-163) include:

Members' persuasive/unpersuasive behaviour. The focal characteristic is the board members' degree of persuasiveness; here persuasive behaviour is not defined as the primary capacity for expression and debate, but is rather connected with a member's credibility level.

Tendency towards disagreement/consensus. Another relevant characteristic is the degree to which a person is inclined to a priori agree or disagree with other members on different issues; practically this means that certain members, regardless of the issue in question and the method of solving it, continually find cause to support or refute a concrete solution.

Individualism/collectivism. As a behavioural characteristic, this indicates the degree of group members' individual performance and their tendency to avoid participation in group discussion; this is closely related to the question of whether board members see themselves as individuals or team players.

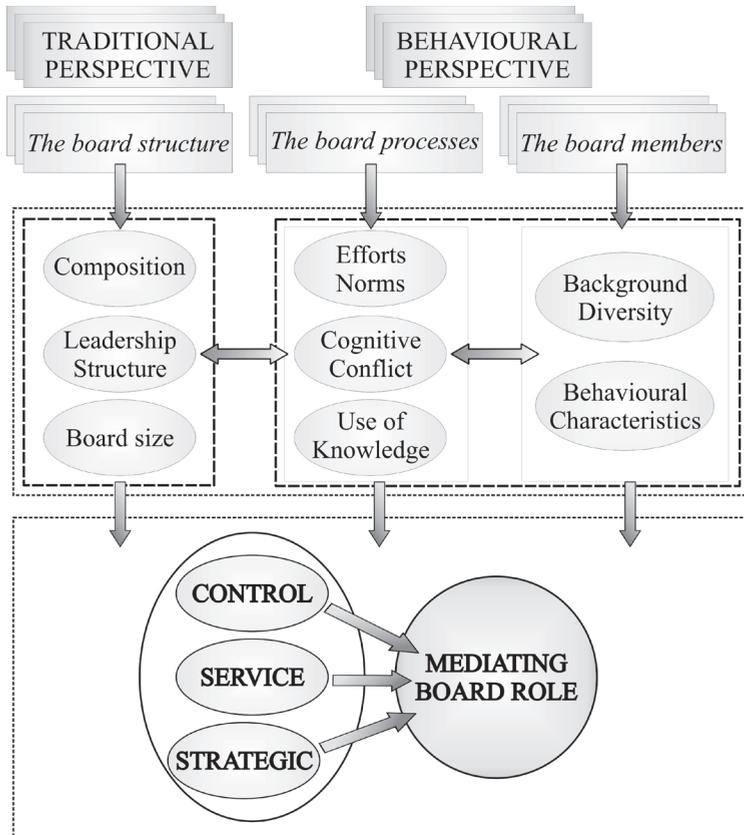
Given the aforementioned behavioural characteristics, ten categories of board member have been identified and divided into two groups: functional and dysfunctional members (Leblanc & Gillies, 2005, pp. 173; Huse, 2007, pp. 212-213). Functional members have a positive impact on board effectiveness because of their expressed skills in building constructive interpersonal relations, communication, and capacity to understand other group members' needs. In addition, they exemplify persuasive behaviour, a high credibility level, and an ability to cooperate successfully with different individuals within and outside the company. Dysfunctional members are dissatisfied members who either criticize others' behaviour with no apparent cause, or continually praise the board chairperson. Hence, they have no opinion of their own and their impact

on board effectiveness is negative. It is thus encouraged that boards contain more functional members that enjoy desirable behavioural characteristics and communication competencies.

#### **4.3. Integrative Model of Board Role Performance**

Studying both structural variables in line with the traditional perspective, and socio-psychological factors influencing a board's behaviour in line with the behavioural perspective, is expected to offer a response to our main research question of why there is a gap between what theory identifies as boards' expectations and the outcomes we see in practice. Addressing this complex issue comes as a result of understanding the key factors of board role performance, i.e., board structure, processes, and individual characteristics of board directors. Board role performance is not merely influenced by formal board structure, but is also affected by interactions and processes within boards. Nonetheless, this does not imply the irrelevance of structural variables, but rather suggests they should be perceived as factors influencing board behaviour. The actual board structure forms a precondition for generating effective relations and interactions among board members. This indicates that comprehensive analysis of factors influencing board role performance needs to include both structural and process variables (Nikolić, 2010). With reference to both traditional and behavioural perspectives, Figure 2 illustrates an integrative model of board role performance, with particular focus on a redefined, mediating board role. Our proposed model encompasses different board effectiveness factors that hitherto were individually analyzed in the context of either traditional or behavioural perspectives.

Figure 2 presents a model for establishing different correlations and identifying research hypotheses that will be tested during the empirical research process. The model suggests that principles of enhanced board effectiveness need to be determined to diminish the existing gap between board role expectations and board role performance.

**Figure 2.** Integrative model of board role performance

Source: Authors' figure

#### 4. CONCLUSIONS AND IMPLICATIONS FOR FUTURE RESEARCH

As the most dominant corporate governance theoretical framework, agency theory has formed the base for abundant empirical research on board performance in the owners' interests with board structure as the key board effectiveness determinant. However, using this method has certain shortcomings. Firstly, the matter of board independence from management has not been sufficiently researched. The concept of board independence is ambiguous and subject to individual interpretation, and therefore significant obstacles in terms of measurement are present. Secondly, the hypothesis on the consensus of board and owner's interests has not been fully confirmed. Thirdly, board members can abuse their power

and act contrary to stakeholders' interests. These shortcomings indicate that the shareholder primacy model based on the agency theory is oversimplified, and that owners in reality have a limited influence on board decisions. As a result the board role is redefined and the director primacy model introduced, based on the stakeholder and stewardship theories. The director primacy model, founded on the corporation role of the board's autonomous fiduciary, should be taken as a starting point in understanding the influence of multi-dimensional factors on board effectiveness.

Traditional research into factors influencing board effectiveness mainly focuses on the limited number of board structural characteristics. This approach proved inadequate, as board structure has no decisive effect on boards' effectiveness. With the development of the behavioural perspective, board effectiveness has been analyzed according to board members' individual characteristics and internal processes. The integrative approach encompassing both research perspectives indicates that structural and process variables are interdependent and their mutual influence determines the degree of board effectiveness.

Nevertheless, board effectiveness models developed in market economies cannot be implemented fully in different legal and economic contexts. Also, development of corporate governance models depends on the individual political system and historical and cultural specificities (Babic, 1998).

In accord with this view, the question is whether the principles of board role performance and effectiveness can be applied in transition economies. The differences in the ownership structure and level of owner concentration (or dispersion) influence the selection and adjustment of corporate control mechanisms. For transition economies the problem of good corporate governance development is complex due to the underdeveloped institutional infrastructure.

Future research will be focused on the identification and analysis of different board roles, relevant to models of corporate governance in transition economies. Considering the fact that the state is the main stockholder, there is an imbalance of power distribution among the various stockholders. Board members are usually representatives of the government, public corporate bodies, or even banks. For individual board members the motivation to act is often inhibited by their relationship with management, due to the fact that their interests are to some extent complementary. Even if they are motivated to exercise direct control over managers, they lack the sufficient knowledge and skills necessary to make managerial decisions. As a consequence the role of the board is reduced

to financial control, which assumes maximization of short-term results and evaluation of the managers' performance ex post. Considering the characteristics of transition economies, underdeveloped financial markets and the strong influence of political power and processes on the decision-making process, the problem of board role performance is still to be investigated, and it is important to answer the following questions: Do the boards in transition economies have the same role as in developed countries? Do the boards have a strategic role at all? Which factors determine board role performance?

Addressing these issues will enhance the overall understanding of board roles, will enable empirical research of factors that influence board role performance, and will, eventually, improve board effectiveness as a corporate governance internal mechanism.

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