THE ROLE OF THE BOARD IN FIRM STRATEGY: INTEGRATING AGENCY AND ORGANIZATIONAL CONTROL PERSPECTIVES*

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Abstract

The role of the board of directors in firm strategy has long been the subject of debate. However, research efforts have suffered from several deficiencies: the lack of an overarching theoretical perspective, reliance on proxies for the strategy role rather than a direct measure of it and the lack of quantitative data linking this role to firm financial performance. We propose a new theoretical perspective to explain the board's role in strategy, integrating organizational control and agency theories. We categorize a board's approach to strategy according to two constructs: strategic control and financial control. The extent to which either construct is favoured depends on contextual factors such as board power, environmental uncertainty and information asymmetry.

Keywords: Strategy; boards of directors; agency theory; organizational control; strategic control; financial control

The Role of the Board in Firm Strategy: Integrating Agency and Organizational Control Perspectives*

Recent media attention highlights that, more than ever, boards of directors are being held accountable for the organizations they govern. High profile corporate collapses, accounting irregularities, corporate corruption, remuneration excesses and inadequate disclosure practices have significantly affected public confidence in markets and focused the media spotlight clearly onto corporate governance (Taylor, 2003). The response has been a significant increase in attention to structural governance solutions, manifest in legislative interventions (e.g. Sarbannes-Oxley Act of 2002 in the US) and in a new round of best practice governance guidelines (e.g. ASX Corporate Governance Council, 2003). These changes have been largely aimed at the conformance role of boards and pay limited attention to the performance role. While company law, governance practitioners and many academics accept that a key aspect of this performance role is board involvement in strategy, there is little consensus on the nature of this involvement, despite considerable debate in the literature.

Early researchers, taking a managerial hegemony perspective, argued that boards made little contribution to strategy (Mace, 1971; Vance, 1983) while others around the same time took the opposite perspective. For example, Boulton (1978) argued that the strategic role of boards was evolving in importance, while Andrews (1980) recommended that directors should work with management in devising strategic plans because of their experience and the fact that an in depth understanding of a firm's strategy facilitated the monitoring function. Lorsch and MacIver (1989: 67) argued that, in the words of one

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director, “the thinking through of where the company is going is underemphasized among directors’ roles”, while the compliance aspects were overemphasized. More recent research has confirmed that directors considered assisting management with making strategic decisions one of their key roles (Conger, Lawler and Finegold, 2001). However, in general, research efforts into the board’s role in strategy have been limited (for a review see Johnson, Daily and Ellstrand, 1996).

This paper addresses this gap in the literature by investigating the strategy role of boards. It is based on three important and inter-related research questions:

1. How do boards fulfil their strategy role?
2. How is this strategy role affected by contextual factors in the firm’s internal and external environments?
3. How does this strategy role relate to firm financial performance?

In addressing these questions we begin by briefly discussing the “active” and “passive” schools of thought that dominate much of the literature on the board’s strategy role. We then discuss the theoretical perspectives that underpin these schools before going on to review the normative and academic literature. We take a chronological approach in reviewing these bodies of work, demonstrating how the conceptualization of the board’s strategy role has developed over time and how this conceptualization is converging in both areas. In synthesizing this literature, we outline the limitations of research efforts to date, particularly (1) the lack of an overarching theoretical perspective on the board’s strategy role, (2) the reliance on proxies for this role rather than a direct measure of it, and (3) the lack of quantitative data linking this role to firm financial performance. Next we present a new theoretical perspective to explain the board’s role in strategy, one that integrates organizational control and agency theories. This integrative perspective draws on the corporate-SBU strategic management literature and argues that boards emphasize a system of strategic (behavioural) controls and financial (outcome) controls over top management and that the extent to which one of these mechanisms is favoured provides an indication of the nature and the degree of board involvement in strategy. We discuss the likely dimensions of these constructs and argue that the firm's context determines the extent to which strategic or financial control is favoured and that the choice of control mechanisms by the board will impact on firm financial performance. We also propose four typologies for the board's strategy role according to the extent to which it emphasizes strategic and financial control. We conclude by discussing the contributions to knowledge of this new theoretical perspective.

TWO SCHOOLS OF THOUGHT

Any discussion of the role of boards of directors relative to strategy needs to begin with a discussion of the concept of strategy itself. However, strategy has become a "catchall term" in the literature with multiple, subjective and often fragmented definitions (Hambrick and Fredrickson, 2001: 48). Whittington (1993) outlined four basic conceptions of strategy – classical, evolutionary, systemic and processual – each of which has very different implications for how to actually "do strategy". Mintzberg, Ahlstrand and Lampel (1998) detailed 10 different schools of thought on strategy, while Kiel and Kawamoto (1997) demonstrated 32 different definitions of the term strategy in the literature. Whittington (1993) also made the point that, in 1993, there were 37 books in print with the title "Strategic Management". Today that number is significantly advanced. Given this diversity of opinion and sheer volume of literature, a detailed discussion of "what is strategy" is well beyond the scope of this paper. However, we have adopted the view of strategy, advocated by Burgelman (1983; 1991) and Noda and Bower (1996), as a shared frame of reference within an organization, providing the basis for an iterative process of objective setting and resource allocation. This view focuses on the "process" of strategy (Mintzberg, 1973; 1978; Mintzberg and Waters, 1985), involves multiple levels within the firm, differentiates between planned or deliberate strategy and emergent strategy, and recognizes that deliberate and emergent strategies "…form the poles of a continuum along which we would expect real-world strategies to fall" (Mintzberg and Waters, 1985: 3).

Having defined strategy, what then is the strategy role of the board? From a legal perspective, the board's fiduciary duty is generally considered to include the review and monitoring of strategy (Stiles and Taylor, 2001). The management literature takes a broader perspective and considers the board's role in strategy to include such aspects as defining the business, developing a mission and vision, scanning the environment and selecting and implementing a choice of strategies (Hilmer, 1993; Pearce and Zahra, 1991; Tricker, 1984). More specifically, Goodstein, Gautam and Boeker (1994: 242) have defined the strategic role of the board as "taking important decisions on strategic change that help the organization adapt to important environmental changes", while Judge and Zeithaml (1992: 771) have defined it as "making nonroutine, organization-wide resource allocation decisions that affect the long term-term performance of an organization".

While there is reasonable consensus in the literature on the board's responsibility for strategy, what has proved difficult to define is how boards fulfil this responsibility (Stiles and Taylor, 2001). The perception often presented by scholars distinguishes between the formulation and evaluation steps in strategy (Judge and Zeithaml, 1992) and posits that boards' involvement in both of these steps can be represented as continua of activity (Pettigrew and McNulty, 1995; Zahra and Pearce, 1989). This thinking has resulted in two broad schools of thought on board involvement in strategy, often referred to in the literature as "active" and "passive" (Golden and Zajac, 2001). The passive school views boards as rubber stamps (Herman, 1981) or as tools of top management (Pfeffer, 1972) whose only contribution is to satisfy the requirements of company law (Stiles and Taylor, 2001). This line of thinking argues that board decisions are largely subject to management control, particularly to that of a powerful chief executive officer (Mace, 1971). On the other hand, the active school sees boards as independent thinkers who shape the strategic direction of their organizations (Davis and Thompson, 1994; Finkelstein and Hambrick, 1996; Walsh and Seward, 1990).

These two schools of thought are supported, at least in part, by managerial hegemony, agency, resource dependence and stewardship theories. In the following section we briefly outline these strategic management theories in the context of the board's strategy role.

THEORETICAL PERSPECTIVES

Managerial Hegemony Theory

Managerial hegemony theory (Lorsch and MacIver, 1989; Mace, 1971; Vance, 1983) argues that boards are a legal fiction dominated by management. As such, they play a passive role in strategy and in the broader sense of directing the corporation. This managerialist perspective relies on five mechanisms for management control. The first was initially expressed by Berle and Means (1932), who argued that the separation of ownership and control in corporations, together with growth in their share capital, leads to a diffuse ownership situation in which the power of large shareholders is diluted. This relative weakness in shareholder control affords management a greater level of control which, based on agency theory, is likely to be self-serving (Jensen and Meckling, 1976) and to place boards in a passive role. A second factor contributing to managerial control, and one which also draws on agency theory (Eisenhardt, 1989), is the information asymmetry between non-executive directors and top management. By the very nature of their internal position, management develop an intimate knowledge of the business, putting the board, and particularly the non-executive directors, at a disadvantage. Third, managers in profitable organizations can reduce their dependence on shareholders for capital and hence enhance their control by using retained earnings to finance investment decisions (Mizruchi, 1983). Fourth, in many cases, "…board members are handpicked by management" (Pfeffer, 1972: 220) and hence, management controls the board by virtue of this appointment process. While this comment applies to both executive and non-executive directors, the presence of executives on the board raises the fifth mechanism for management control. Namely, since inside directors report to the chief executive officer and are largely dependent on this person for compensation and career advancement, the extent to which such directors occupy board seats is likely to confer a power imbalance to the chief executive (Stiles, 2001). The net effect of these five control mechanisms is that strategy is the province of the chief executive and the senior management team and boards only play a review and approval role, a "rubber-stamp" function (Herman, 1981). This passive role for boards in strategy is also implicit in the strategic management literature according to Ingley and Van der Walt (2001), while

McNulty and Pettigrew (1999: 50) argue that this body of literature is "largely silent on boards' involvement in strategy".

Critics of managerial hegemony theory argue that its empirical support is limited (Stiles and Taylor, 2001) and that its theoretical basis is dependent on the definition of the term "control". For example, Mizruchi (1983) argues that the board has ultimate control over management through their capacity to hire or fire the CEO. Furthermore, Zeitlin (1974) argues that increasing concentration of firm ownership by large investors and the growth of interlocking directorships considerably reduce managerial power. Kiel and Nicholson (2003) pose a similar argument, citing the increasingly independent role of the board in both control and direction since the 1980s.

Agency Theory

Agency theory focuses on the notion of an agency relationship in which the principal delegates work to the agent, there is risk sharing between the entities and there is potential conflict of interest (Eisenhardt, 1989). It assumes that agents are opportunists who operate with bounded rationality – they will self satisfice rather than profit maximize on behalf of the principal (Eisenhardt, 1989). Agency theory argues that the major role of the board is to reduce the potential divergence of interest between shareholders and management, minimizing agency costs and protecting shareholders' investments. Agency theory has very clear implications for the monitoring and control role of the board (Eisenhardt, 1989), but its position regarding the strategy role is not as definite. However, Zahra and Pearce (1989: 302) argue that agency theory emphasizes the crucial importance of the board's role in strategy, stating that it:

> …places a premium on a board's strategic contribution, specifically the board's involvement in and contribution to the articulation of the firm's mission, the development of the firm's strategy and the setting of guidelines for implementation and effective control of the chosen strategy.

These scholars also acknowledge that there is "little documentation" to support this contention (Zahra and Pearce, 1989: 303). Similarly, McNulty and Pettigrew (1999: 50) argue that "little has been said by agency theorists about strategy as a means of control over managers". However, these scholars also suggest that, within the context of a broad perspective on the meaning of corporate control (Hill, 1995), agency theory does have implications for the strategy role of boards. This argument perceives control as going past constraints on management designed to reduce divergence of interests with shareholders. It sees control as a mechanism to shape the strategic direction of organizations (Stiles and Taylor, 2001).

Stewardship Theory

Stewardship theory (Davis, Schoorman and Donaldson, 1997) argues against the opportunistic self-interest assumption of agency theory, claiming that managers are motivated by "a need to achieve, to gain intrinsic satisfaction through successfully performing inherently challenging work, to exercise responsibility and authority, and thereby gain recognition from peers and bosses" (Donaldson, 1990: 375). This perspective recognizes a range of non-financial motives for managerial behaviour and it supports the active school, arguing that the strategic role of the board contributes to its overall stewardship of the company (Hung, 1998; Stiles, 2001). It also argues that insider dominated boards contribute a depth of knowledge, expertise and commitment to the firm which facilitates an active strategy role (Muth and Donaldson, 1998).

Resource Dependence Theory

Resource dependence theory stems from research in economics and sociology and focuses on the role of interlocking directorates in linking firms to both competitors and other stakeholders (Zahra and Pearce, 1989). According to this theory, boards are a "co-optative" mechanism for a firm to form links with its external environment, to access important resources and to buffer the firm against adverse environmental change (Goodstein *et al*., 1994; Pearce and Zahra, 1991; Pfeffer, 1972, 1973; Pfeffer and Salancik, 1978). However, as with agency theory, the implications of resource dependence theory for the strategy role of boards are mixed. While Stiles (2001) argues that the board's boundary spanning activity contributes to the strategy role by bringing in new strategic information, others (Finkelstein and Hambrick, 1996; Hung, 1998; Stiles and Taylor, 1996) argue that resource dependence theory focuses on the role of boards in attaining resources rather than using such resources. For example, Carpenter and Westphal (2001: 639) suggest that boards serve as "a strategic consultant to top managers rather than (or in addition to) exercising independent control".

To summarize, the passive school is underpinned by managerial hegemony theory, while the active school relies on stewardship, agency and resource dependence theories. In the following sections the application of these theories in the normative and academic literature is reviewed. We take a chronological approach to demonstrate how thinking on the board's role in strategy has developed over time and how this thinking is converging towards a common viewpoint by both practitioners and academics.

NORMATIVE LITERATURE

Following Mace's (1971) seminal study, *Directors: Myth and Reality*, in which he found that boards typically only became involved in strategy at times of crisis, the normative literature made a clear call for more active involvement (e.g. Brown, 1976; Felton, 1979; Groobey, 1974; Mueller, 1978). However, 10 years later "…director participation in strategic decisions had not flourished" (Andrews, 1981: 174). Hosting a debate in the *Harvard Business Review* on strategy as a vital function of the board, Andrews (1981) identified five key issues that he believed were delaying productive board participation in strategy. First, he argued that it was not the board's role to formulate strategy, but rather to review it and monitor the process that produces it. Second, the definition of strategy and to what extent it should be articulated were not well understood by boards. Third, chief executives constrained the board's involvement in strategy. Fourth, outside directors were not well enough informed about the intricacies of the company's business to be able to review and evaluate strategic recommendations. Fifth, boards were unwilling to become involved in making long-term decisions characterized by risk and uncertainty. What is interesting about Andrew's observations is that, some twenty years later, the same issues continue to surface (Golden and Zajac, 2001; McNulty and Pettigrew, 1999; Oliver, 2000; Stiles, 2001).

The 1980s only saw limited advances in understanding of the strategic role of boards. The focus during this time was on boards' involvement in strategic planning (e.g. Henke, 1986; Tashakori, Boulton and Lauenstein, 1983), the role of institutional investors (Dobrzynski *et al*., 1988; Power, 1987), the influence of the courts (Galen, 1989; Glaberson and Powell, 1985) and the market for corporate control (Weidenbaum, 1985), each of which advocated a more active strategic role for boards. However, an important development in the US during this period was the implementation by the New York Stock Exchange in 1984 of the audit committee rule, which required that these committees be comprised entirely of outside directors. The net effect was that outsiders typically exceeded insiders on the boards of large firms and, because of their external commitments and limited understanding of the firm; the argument continued that directors had limited involvement in strategy (Patton and Baker, 1987; Whisler, 1984).

The 1990s saw a surge of interest in boards of directors, largely generated by the corporate excesses of the prior decade (McNulty and Pettigrew, 1999). Boards came under increasing scrutiny from regulators, from shareholders, particularly large institutions, and from an expanding complement of stakeholders (Ingley and Van der Walt, 2001). Codes of conduct and corporate governance guidelines were developed (Committee on the Financial Aspects of Corporate Governance, 1992; Bosch, 1995; Hampel, 1998; Toronto Stock Exchange Committee, 1994) which focused strongly on compliance and accountability. However, while practitioners recognized the importance of an increased "conformance" role for boards, several also called for a balancing emphasis on "performance" (Blake, 1999; Tricker, 1994) driven by a stronger strategic role. Pound (1995) called for the adoption of the 'governed corporation' model in which the focus was on organizational performance through board-management collaboration.

Addleman (1994) and Walker (1999), focusing on self-assessment of performance by boards, argued that significantly more time needed to be spent on strategic rather than operational issues. Walker (1999) argued that the board should periodically review the firm's mission, values and vision; make policy and strategic decisions that support the mission, values and vision; be involved in strategic planning; approve goals and objectives; and measure management's progress against these goals and objectives. Other practitioners also focused on the board's role in strategic direction. For example, Tricker (1999) stressed the importance of this role in the development of corporate goals, while Rhodes (1999) maintained that boards should establish a focused, cohesive company mission and review the implementation of strategic initiatives to meet company objectives. Helmer (1996) asserted that the board's role in strategy was to establish standards, counsel the CEO, approve and review strategy development against these standards and monitor strategy implementation.

Other practitioners have focused more on the process of strategy itself, arguing that the appropriate role for boards is strategic thinking (Dilenschneider, 1996; Garratt, 1996) or strategic leadership (Davies, 1999). Strategic thinking, according to Garratt (1996), is concerned with long-term organizational effectiveness and involves strategic analysis, strategy formulation and setting corporate direction. Strategic leadership, according to Davies (1999), requires a board with a balance of strategic skills and experience relative to the needs of the firm, with a shared strategic direction and commitment to pursue it, and strong processes to effect strategic management. Hence, both notions sit towards the active end of the strategy continuum (Ingley and Van der Walt, 2001).

Further support for a more active role for boards in strategy comes from the OECD's (1999: 9) *Principles of Corporate Governance*, which state that, "The corporate governance framework should ensure the strategic guidance of the company…" In addition, themes established in the prior decade continued to provide support for the active school. For instance, the courts reinforced the view that boards should take an active role in strategy (Baxt, 1999; Bosch, 1995), while institutional investors also continued to push for a more active strategic role on the part of boards (CalPERS, 2000; TIAA-CREF, 2000).

Recent media attention has focused on the monitoring role of boards (e.g. George, 2002) and has led to a plethora of "best practice" recommendations (e.g. ASX Corporate Governance Council, 2003; NACD, 2000; OECD, 1999) and legislative intervention (e.g. Sarbanes-Oxley Act of 2002). This renewed focus on the conformance role has again sparked the concern that boards may not be adequately emphasising their performance role (Lahey, 2003). In this sense, the conformance – performance debate is returning to that held in the last decade (Pound, 1995; Tricker, 1994).

What becomes apparent from this discussion is that the normative literature clearly favours a more active role for boards in strategy. However, one key question is how active should boards be? The distinction between setting and monitoring strategic direction, and executing strategies on an operational level has become increasingly blurred (Ingley and Van der Walt, 2001) and boards run the risk of stepping into what should be management's responsibilities (Helmer, 1996). This is a particular concern relative to the board's role in developing strategy. One perspective argues that the board should participate as an equal partner with management (Dimma, 1997), while another suggests that the board should only provide oversight in this area (NACD, 2000). Another key point of debate is whether boards, particularly those comprised predominantly of non-executive directors, have sufficient insight into the fundamentals of the business to provide a significant strategic contribution (Helmer, 1996).

To summarize, while there is clear convergence in the normative literature that boards have a definite role to play in strategy, there is still debate on the nature of that role (Helmer, 1996). An implicit point in this convergence is that there is a clear link between the board's involvement in strategy and organizational effectiveness (e.g. Committee on the Financial Aspects of Corporate Governance, 1992). However, this link has not been clearly established empirically, a point which will be elaborated in the following section on the academic literature.

ACADEMIC LITERATURE

The convergence of opinion in the normative literature for an active role of boards in strategy is not as clearly reflected in the academic literature. Despite considerable scrutiny from researchers, there is little consensus on the behavioural dynamics of boards and on how they impact on the development and execution of firm strategy (Golden and Zajac, 2001; McNulty and Pettigrew, 1999). The research efforts that have developed from the active and passive schools have followed different agendas and led to different conclusions (Golden and Zajac, 2001). In fact, Rindova (1999) has described the evolution of research on boards and strategy as following a dialectical sequence from a thesis that managers dominate directors to an antithesis that directors should control managers. We demonstrate this sequence in the remainder of this section by briefly reviewing empirical and theoretical studies, beginning with those in the managerialist tradition and then focusing on more recent research advocating the "active" school of thought.

Managerial hegemony theory found early expression in the work of Berle and Means (1932), but it was Mace's (1971) study that set the agenda for the passive school of thought. He interviewed fifty directors of medium and large US corporations and found that boards only impacted on strategic decision making in times of crisis and that they were otherwise controlled by chief executive officers. Other scholars followed Mace's approach with similar results (Norburn and Grinyer, 1974; Pahl and Winkler, 1974; Rosenstein, 1987), concluding that boards provided little strategic direction and that this role rested primarily with the chief executive officer. Recognising that these results were largely driven by the power imbalance between management and boards, the latter were termed "creatures of the CEO" (Mace, 1971) who served merely a rubber-stamping function (Herman, 1981).

Lorsch and MacIver (1989), in their well known text *Pawns or Potentates: The Reality of America's Corporate Boards*, came to similar conclusions as Mace (1971). However, rather than frame boards as rubber stamps or creatures of the CEO, these scholars positioned them in a more positive sense, finding that their primary role in strategy was to advise the chief executive officer, providing counsel on the evaluation of options rather than initiating strategy. Nonetheless, their work, while recognising the progress made by a small number of boards, reinforced the passive school of thought explained by managerial hegemony theory.

While this early body of research was clearly sceptical about the board's role in strategy, other researchers were developing a somewhat different, although not always conclusive, perspective. Tricker (1984) argued that boards were involved in the formulation of strategy but that this involvement was approached largely from the perspective of internal firm issues rather than shareholder interests. In a survey of 234 large US corporations on board involvement in strategic planning, Henke (1986) concluded that such involvement had improved since Mace's (1971) study, but that boards were still "not adequately meeting their responsibilities of providing long-term direction to their firms" (Henke, 1986: 95). Further support for the active school came from Hill and Snell (1988), who focused on research intensive industries and found that boards impacted on the choice between innovation and diversification strategies.

Research in the early 1990s continued to position the strategic role of boards in a more active light. Survey research by Demb and Neubauer (1992) with UK and European companies found that 75% of respondents considered setting strategy as the main function of boards. However, qualitative research by these scholars demonstrated that the degree of board involvement was dependent on the strategy formation process and the relative power of the chief executive vis-à-vis the board – a more emergent strategy formation process was associated with a more powerful chief executive officer and less influence by the board on strategy.

Survey studies conducted with both US and European companies showed that a significant proportion of boards considered themselves to be actively engaged in the choice of strategic options and that a median figure of 25% of board meeting time was devoted to strategy issues (Bacon, 1993; Berenbeim, 1995). However, while these studies demonstrated a growing recognition of the importance of boards' involvement in strategy, they did not address the nature of this involvement. Insight into this aspect came from Demb and Neubauer (1992: 55) who proposed three archetypes for boards based on their overall role portfolio – the Watchdog, the Trustee and the Pilot – and elaborated these characterisations relative to the strategy role. The Watchdog board focuses primarily on monitoring and evaluating strategy post-implementation; the Trustee board plays a limited role in the initiation of strategy, but a substantive role in analysing options, monitoring and evaluating results; and the Pilot board plays a more substantive role in all areas. These scholars characterized this progression of involvement as a continuum, a notion that subsequently gained prominence in the normative literature (Ingley and Van de Walt, 2001).

Other researchers have also focused on the nature of boards' involvement in strategy. In a review of the corporate governance literature over the prior 25 years, Zahra and Pearce (1989) argued that an active strategy role for boards involved counsel and advice to the chief executive officer, initiation of strategic analyses and suggestion of strategic alternatives. Similarly, Hermalin and Weisbach (1988) found that chief executives relied on directors for input in the formulation of strategy. Ferlie, Ashburner and Fitzgerald (1994) reinforced the continuum concept, identifying three levels of board involvement: (1) rubber stamp, (2) probing and questioning of strategic options and (3) active participation in deciding between options, including shaping the vision. Taking a sociological perspective, Hill (1995) established that non-executive directors perceived strategic direction as their main purpose, one which involved bringing breadth of vision, environmental scanning and acting as a sounding board for the chief executive.

Indirect evidence of the board's role in strategy may be found in research investigating the diffusion of innovations through interlocking directorates. For example, Davis (1991) found that poison pill anti-takeover provisions diffused through interlocking directorates, while Johnson, Daily and Ellstrand (1996) have suggested that the diffusion of the multi-divisional corporate structure (Palmer, Jennings and Zhou, 1993) or general acquisition strategies (Haunschild, 1993) may provide evidence for an active role of directors in strategy.

Recent research has continued to challenge the managerialist perspective and to elaborate how boards play an active role in firm strategy. For instance, the contribution to strategy by chairmen and non-executive directors in large UK public companies has been examined using data gathered from interviews with 108 company directors (McNulty and Pettigrew, 1999). These scholars conceive of strategy in terms of capital investment proposals, which they suggest are "…about acquiring another firm, embarking on a joint venture, merging businesses or disposing of a business operation" and which " may reflect broader strategic intentions relating to growth and diversification of business activities" (McNulty and Pettigrew, 1999: 56). McNulty and Pettigrew (1999) also focused on both the content and the process of board involvement in strategy. Their results indicate that non-executive board members rarely initiate the substantive content of strategy, the exceptions being firms in crisis or poor performance and firms that had previously been state owned. However, McNulty and Pettigrew (1999) did demonstrate that non-executive board members had three levels of involvement in strategy which they termed (i) taking strategic decisions, (ii) shaping strategic decisions and (iii) shaping the context, conduct and content of strategy. These three levels are summarized in Table 1 and explained in the following.

INSERT TABLE 1 ABOUT HERE

"Taking strategic decisions" is defined as the exertion of influence by the board at the end of the capital investment decision process. The board behaviour involved is either acceptance, rejection or referral back to management for changes of capital investment proposals and, according to McNulty and Pettigrew (1999), all boards are involved in this behaviour.

The second level, termed "shaping strategic decisions", involves the exercise of influence by non-executive board members early in the decision process, effectively shaping the preparation of capital investment proposals by management. The board behaviour involved at this level covers two kinds of processes. First, management may directly consult non-executive directors, either formally or informally, during the preparation of proposals. Second, executive directors may anticipate the response of the full board and self-regulate proposals before they go to the board for the "decision taking" stage. Hence, while "taking strategic decisions" is grounded in the control role of agency theory (Eisenhardt, 1989) and occurs all the time, "shaping strategic decisions" can be considered as a more consultative form of control (McNulty and Pettigrew, 1999).

The third level of strategy involvement demonstrated by McNulty and Pettigrew (1999), "shaping the context, conduct and content of strategy", goes beyond these notions of control and is defined as a continuous process of influence by non-executive directors. It can be better understood by reference to each of the terms context, conduct and content. Context refers to the conditions under which the strategy process happens in firms. For example, is strategy deliberate, emergent or a mix of both? Is strategic thinking a legitimate and valued activity in the boardroom? Is strategy debated openly at board level? Conduct refers to the processes used to develop strategy at both board and management level as well as the implementation processes at management level. While there is some overlap between the context and conduct of strategy at board level, non-executive directors may also shape the strategic conduct of management by specifying behaviour such as the submission of board papers, by establishing a process for developing strategy and monitoring the execution of that process and by establishing a clear framework of strategic responsibilities for management. Finally, boards shape strategic content by asking management to justify their intentions, by evaluating alternatives and by monitoring progress. Hence, this third level of strategy involvement involves the board developing the context for strategic debate, establishing a methodology for strategy development, monitoring strategy content and controlling the conduct of management relative to strategy. Support for the significance of this level of strategy involvement comes from Pye (2001), who argues that having a continuous process of dialogue and debate on strategy at board level is as important as the content of that strategy.

McNulty and Pettigrew's (1999) results indicate that only a minority of boards shape the context, conduct and content of strategy. Interestingly, they argue that the ultimate step in this third level of strategy involvement is firing the chief executive. In fact, they suggest that all three levels of strategy involvement represent a controlling influence over management that is consistent with agency theory. They also suggest that the processes of control and choice, particularly those evident in levels two and three, reflect a resource dependence perspective in that they involve boards drawing upon their knowledge and experience in influencing management.

In another pivotal study demonstrating the active role of UK public company boards in strategy, Stiles and Taylor (2001) employed an approach involving in depth interviews with 51 directors and 4 case studies. Their results indicated that the board's role was not to formulate strategy, but to set the strategic context and to maintain the strategic framework. The first mechanism involves defining what business the firm is in, setting its vision and values and is conceptually very similar to McNulty and Pettigrew's (1999) notion of shaping the context of strategy. Maintaining the strategic framework has three key dimensions: (1) gatekeeping, a process in which strategic proposals are actively reviewed and often changed through feedback and advice, (2) confidence building, a process in which boards encourage entrepreneurial activities by management, and (3) selecting appropriate directors, especially the CEO. We contend that this second mechanism is conceptually similar to McNulty and Pettigrew's (1999) notions of shaping the content and conduct of strategy.

Hence, as with McNulty and Pettigrew (1999), Stiles and Taylor's (2001) research has demonstrated that UK boards play an active role in strategy, which further challenges the managerialist perspective. Interestingly, both studies indicated that, while boards rarely formulated strategy, except in crisis conditions, their strategic involvement could be described along some form of activity continuum. This progression of involvement raises an interesting question: what are the factors, besides crises, that influence the extent and nature of boards' involvement in strategy?

Early studies on this theme were largely qualitative, identifying factors such as the will, experience, expertise and confidence of directors, particularly non-executives (Ferlie *et al*., 1994; Pettigrew and McNulty, 1995); the extent to which the chair wants the board involved (O'Neal and Thomas, 1995); the relative power of management vis-à-vis the board (Ferlie *et al*., 1994); the degree of information asymmetry between the board and management (O'Neal and Thomas, 1995); and changing board dynamics (Pettigrew and McNulty, 1995).

In an important contribution to the literature, McNulty and Pettigrew (1999) drew on their interviews with UK directors to suggest a number of contextual and processual influences on boards' involvement in strategy. These scholars deliberately focused on factors other than board composition and structure and argued that the interplay between these multiple influences is critical to understanding the conditions that facilitate or restrict non-executive directors' involvement in strategy. Contextual factors include changing societal norms and the history and performance of the firm (McNulty and Pettigrew, 1999; Zald, 1969). Processual factors suggested by McNulty and Pettigrew (1999) include the agenda for board meetings, the process and conduct of meetings, the use of strategy "away-days" and informal dialogue between directors outside of board meetings.

Quantitative studies of the factors that influence the extent and nature of boards' involvement in strategy have addressed aspects such as board demographics (Baysinger, Kosnik and Turk, 1991; Golden and Zajac, 2001; Hill and Snell, 1988), ownership by institutional investors (Baysinger *et al*., 1991), prior firm performance (Westphal and Fredrickson, 2001), board power (Alexander, Fennell and Halpern, 1993; Golden and Zajac, 2001), board interlocks and firm environment (Carpenter and Westphal, 2001). It is important to note that the dependent variable in these quantitative studies has generally been some measure of strategic change as a proxy for the board's strategy role. Such measures have included innovation (Baysinger *et al*., 1991; Hill and Snell, 1988), diversification (Hill and Snell, 1988; Westphal and Fredrickson, 2001), and capital investment and services provision in hospitals (Beekun, Stedham and Young, 1998; Golden and Zajac, 2001; Goodstein *et al*., 1994).

While these quantitative studies have provided valuable insight into the factors likely to affect board involvement in strategy, they have not clarified the implicit assumption in the normative literature that board involvement in strategy is clearly linked to organizational effectiveness, particularly financial performance (e.g. Committee on the Financial Aspects of Corporate Governance, 1992). Empirical efforts have largely concentrated on the link between various measures of board demographics, rather than board roles, and firm financial performance and have found little evidence of any systematic relationship (e.g. Dalton, Daily, Ellstand and Johnson, 1998; Dalton, Daily, Johnson, and Ellstrand, 1999; Rhoades, Rechner and Sundaramurthy, 2000). Other studies have concentrated on strategic decision making by boards in areas such as anti-takeover tactics (e.g. Rechner, Sundaramurthy and Dalton, 1993; Sundaramurthy, Mahoney, and Mahoney, 1997), golden parachutes (Cochran, Wood, and Jones, 1985; Davidson, Pilger and Szakmary, 1998; Wade, O'Reilly and Chandralat, 1990), greenmail (Kosnik, 1987) and poison pills (Brickley, Coles and Terry, 1994; Davis, 1991; Mallette and Fowler, 1992). While many of those studies do relate strategic decision making to financial performance, they are generally episodic in nature and provide little insight into the antecedent behaviour of the boards involved.

More focused efforts have shown that "participative" boards, defined in part by their strategy involvement, were associated with superior financial performance (Pearce and Zahra, 1991). Other such efforts have also shown a positive but weak relationship between board involvement in strategy and firm financial performance (Judge and Zeithaml, 1992).

To conclude this section, the academic literature demonstrates a swing from the passive school of the 1970s and 1980s to the active school prevalent over the last ten years. The support for this swing, while limited, derives from both qualitative and quantitative research. The former has largely relied on director interviews and case studies and has provided clear support for the active school as well as excellent insight into how boards carry out their strategy role. These studies have also suggested a number of important contextual and processual influences on this role. Unfortunately, quantitative research efforts to date, while supportive of the qualitative results, have not been as lucid. These studies have largely relied on surveys with limited participation and on archival data. The independent variable has generally been some measure of board demography and board involvement in strategy has often been represented by various measures of strategic change as proxies for the dependent variable. Despite the shortcomings, these studies have provided support for the active school as well as further insight into the factors likely to affect board involvement in strategy. With the exception of two studies (Pearce and Zahra, 1991; Judge and Zeithaml, 1992), the quantitative literature has not demonstrated a link between board involvement in strategy and firm financial performance.

SYNTHESIS OF THE NORMATIVE AND ACADEMIC LITERATURE

A number of conclusions can be drawn from this review of the normative and academic literature. First, the early managerialist perspective which saw boards as “rubber stamps” has been slowly overtaken by an “active” perspective, which sees boards more as independent thinkers who shape the strategic direction of their organizations. While we recognize that this strategy role of boards is still the subject of debate, we suggest that an appropriate definition, based on this active perspective, is that it is an iterative process of non-routine resource allocation decisions that help an organization adapt to environmental changes (Mintzberg, 1983; Pearce and Zahra, 1991; 1992; Zald, 1969) and that contribute to organizational performance (Judge and Zeithaml, 1992; Goodstein *et al*., 1994).

Second, the literature is only just beginning to elaborate the behavioural dynamics of boards and their impact on firm strategy (Golden and Zajac, 2001; McNulty and Pettigrew, 1999; Stiles, 2001). There is limited consensus on how boards actually go about their strategy role and no overarching theoretical perspective that adequately explains this role. We argue that conceiving of boards' involvement in strategy as a continuum from "active" to "passive" (Demb and Neubauer, 1992) is an oversimplification. The passive conception assumes that strategic decisions are both separate and sequential: managers generate options from which boards choose; managers then implement the chosen option and boards evaluate the outcomes (Fama and Jensen, 1983; Rindova, 1999). The active conception assumes that boards and management formulate strategy in a partnership approach, management then implements and both groups evaluate (Demb and Neubauer, 1992; Ingley and Van de Walt, 2001). However, strategic decisions often evolve through complex, non-linear and fragmented processes (Cohen, March and Olsen, 1972; Hickson, Butler, Cray, Mallory and Wilson, 1986; Mintzberg, Raisinghani and Theoret, 1976). A board could be actively involved in strategy without being involved in its formulation. For example, a board could "shape" strategy through a process of influence over management in which it guides strategic thinking (McNulty and Pettigrew, 1999), but never actually participate in the development of strategies in the first place.

Third, given this limited attention to the behavioural dynamics of boards relative to strategy, it is not surprising that quantitative research efforts have often relied on variables "at one remove from board activity" (Stiles and Taylor, 2001: 21). The independent variable has generally been some measure of board demography. The dependent variable, board involvement in strategy, has generally been represented by various measures of strategic change as proxies rather than by a direct measure.

Fourth, there is an implicit normative assumption that board involvement in strategy is positively linked to organizational effectiveness. However, the empirical evidence to support this assumption is very limited. While there is a suggestion in the literature that board involvement in strategy is associated with improved financial performance (Judge and Zeithaml, 1992; Pearce and Zahra, 1991), most of the empirical studies have focused on episodic strategic decisions related to events such as anti-takeover tactics. As such, they have provided little insight into the strategy-performance link.

Fifth, a number of studies have indicated that certain contingencies provide for a more influential strategy role for the board. For instance, at times of crisis such as a sudden decline in performance, CEO succession or some other major organizational change, boards become more actively involved in strategy (McNulty and Pettigrew, 1999; Stiles, 2001; Westphal and Fredrickson, 2001; Zald, 1969). Besides these significant episodes, there are a range of other internal and external contingency factors that affect board involvement in strategy. Internal contingencies include various measures of board demographics such as the proportion of insiders (Baysinger *et al*., 1991; Hill and Snell, 1988), directors' skills and experience (Westphal and Fredrickson, 2001), board size (Goodstein et al., 1994), occupational diversity (Golden and Zajac, 2001; Goodstein *et al*., 1994), board tenure and board member age (Golden and Zajac, 2001). Other internal contingencies include firm size and life cycle (Daily and Dalton, 1992; 1993), board attention to strategic issues (Golden and Zajac, 2001), board processes such as the use of strategy "away-days" (McNulty and Pettigrew, 1999), prior firm performance (McNulty and Pettigrew, 1999; Stiles, 2001; Westphal and Fredrickson, 2001) and the relative power between the board and the chief executive officer, particularly in terms of board involvement in monitoring and evaluation of this position (Golden and Zajac, 2001). External contingencies include changing societal norms (McNulty and Pettigrew, 1999), concentration of ownership (Baysinger *et al*., 1991), and environmental turbulence (Golden and Zajac, 2001; Goodstein *et al*., 1994). Consideration of the breadth of these contingency factors suggests that their likely impact on the board's role in strategy is both complex and dynamic.

We suggest that the lack of an overarching theory on the board's strategy role, the reliance on proxies for this role rather than a direct measure of it and the lack of quantitative data linking this role to firm financial performance represent major gaps in the research agenda. In the following section we develop an integrative theory to address these gaps.

AN INTEGRATION OF ORGANIZATIONAL CONTROL AND AGENCY THEORIES

Although managerial hegemony, stewardship, agency and resource dependence theories provide insights into the strategy role, no single perspective adequately explains this role (Stiles and Taylor, 2001). However, each theoretical perspective supports the view of the board as a broad control mechanism (Stiles and Taylor, 2001) and in the remainder of this section we build on this control focus, developing an overarching theoretical perspective to explain the board's strategy role. This argument perceives control as going beyond board constraints on management designed to reduce divergence of interests with shareholders. It sees control as a broad mechanism to shape mission and vision, to regulate "the capacity for innovation and entrepreneurship" and to facilitate boards "breaking organizational habits and forcing change" (Stiles and Taylor, 2001: 52).

Our approach is based on the initial work of Baysinger and Hoskisson (1990) and Beekun, Stedham and Young (1998), who integrated organizational control and agency theories to explain the board's role in strategy. Recognizing that there are two broad forms of control systems in diversified corporations – financial control and strategic control (Goold and Quinn, 1993; Gupta, 1987; Hitt, Hoskisson and Ireland, 1990) – these scholars argued that there is a parallel between these control systems and those exercised by boards over top management. Baysinger and Hoskisson (1990) defined strategic or behaviour control as involving a subjective assessment of strategic decisions pre-implementation as well as an objective assessment of financial performance post-implementation. Conversely, they defined financial or outcome control as involving primarily, if not solely, financial performance post-implementation. Support for this argument has come from empirical research by Beekun, Stedham and Young (1998: 14), who demonstrated that “the board’s choice of controls for top management is an important link between corporate boards and corporate strategy”.

Focusing on the application of strategic and financial control by boards, traditional behavioural perspectives (Finkelstein and Hambrick, 1996: 228) have been “virtually uniform” in their assumption that “boards of directors are not involved in strategy formation”. This school of thought sees boards exercising financial control over top management by monitoring financial results and occasionally firing or otherwise disciplining executives for poor firm performance (Kosnik, 1987; Warner, Watts and Wruck, 1988; Weisbach, 1988). Strategic control, according to this school, is generally reserved for executives, not boards (Hoskisson, Johnson and Moesel, 1994; Zajac, 1990). This traditional, “passive” perspective sees the board’s role in strategy as firing a poor performing CEO and selecting a new one who can bring a fresh perspective on strategic opportunities and determine a new strategic direction for the firm (Westphal and Fredrickson, 2001). However, as previously outlined, there is a substantive body of research which indicates that, while CEO replacement is a key event, boards also influence corporate strategy through mechanisms such as shaping mission, vision and values, establishing the boundaries of strategic activity and scanning the environment for trends and opportunities (e.g. McNulty and Pettigrew, 1999; Stiles and Taylor, 2001). We contend that these mechanisms can be conceived of as strategic control.

Boards exercise a system of both strategic and financial control and that these dimensions of control are analogous to those outlined in the corporate-SBU management literature. Using McNulty and Pettigrew’s (1999) approach to clarify our argument we argue that boards that emphasize strategic control favour a behaviour control role in strategy. In other words they shape (1) the context of strategy by setting the conditions under which the strategy process happens in firms, (2) the content of strategy by requiring that management justify their intentions, by evaluating alternatives and by continuously monitoring progress during this formulation and assessment stage, and (3) the conduct of strategy by continuously monitoring implementation and results and by making changes where appropriate. Strategic control involves the board exerting a continuous process of formal and informal influence over management, beginning early in strategy development and involving iterative consultation from development through to implementation and evaluation. It also involves the board evaluating management based on their strategic proposals pre-implementation as well as on the financial results post-implementation.

Our description of strategic control also fits well with the strategy and control roles described by Stiles and Taylor (2001). While strategy and control are presented as separate roles, Stiles and Taylor (2001: 61) also acknowledge "that the seeming conflict between the board's strategic role and the control is more apparent than real, and, indeed, that the distinction between the two roles is blurred". The authors identify two distinct forms of control within the strategy role: the framing of corporate values and establishing the boundaries of strategic activity. Furthermore, they identify two facets to the control role of the board: "control as diagnosis" in which the board uses "the control systems of the firm to set new strategic direction" and "control as assessment" in which the board assesses the performance of executives, including the use of incentives and sanctions (Stiles and Taylor, 2001: 61).

Turning to financial control, we argue that boards that emphasize this form of control favour an "outcome" role in strategy. In other words they set financial targets only and take strategic decisions relative to these targets by approving, rejecting or referring strategic proposals back to management. Financial control involves the board exerting episodic influence over management at formal board meetings and only at the end of the resource allocation decision process. It also involves the board evaluating management primarily on the financial results of the firm.

Qualitative research into corporate strategy suggests that strategic control and financial control are points along a continuum (Goold, Campbell and Alexander, 1994). However, research grounded in agency theory views behaviour control and outcome control as dichotomous variables (Anderson, 1985; Eisenhardt, 1985, 1988). As a result, we have assumed a dichotomy for strategic and financial control and have developed a typology for characterizing a board's strategy role based on these two constructs (Figure 1).

INSERT FIGURE 1 ABOUT HERE

As Figure 1 highlights, a board can be classified into one of four "strategic types" according to its relative emphasis on strategic and financial controls. A board that emphasizes neither strategic nor financial controls would be classed as a "rubber stamp" board, representing the managerial hegemony perspective (Lorsch and MacIver, 1989; Mace, 1971; Vance, 1983). Conversely, a board that emphasizes both strategic and financial controls would be heavily involved in operations and would be classed as a de facto management team. A strategic control board will emphasize behaviour controls rather than outcome controls, while the converse will be true for a financial control board. We argue that the relative emphasis between strategic and financial control is dependent on the firm and board context as outlined in the following section.

TOWARDS A CONTINGENCY FRAMEWORK

The relative emphasis between strategic and financial controls in the corporate-SBU literature depends on the organization's context (Baysinger and Hoskisson, 1989; 1990; Gupta, 1987). This contingency perspective recognizes factors such as task programmability and outcome measurability from organizational control theory (Eisenhardt, 1985, 1989) and differing attitudes to risk on the part of principal and agent, goal conflict between principal and agent, information asymmetry and outcome uncertainty from agency theory (Eisenhardt, 1989). In a similar manner, we argue that these contextual factors also impact on the board's relative emphasis on strategic versus financial controls over top management. In particular, we have developed propositions around three key contingencies and used these to develop a final proposition around firm performance (see Figure 2).

INSERT FIGURE 2 ABOUT HERE

The first of these contingencies is board power or the relationship between the board and the top management team, particularly the CEO (Westphal, 1999; Westphal and Fredrickson, 2001). Powerful top executives (Finkelstein, 1992) are able to use this power to assume implicit control over directors and may be able to influence board involvement in strategy (Johnson, Hoskisson and Hitt, 1993). In addition, there is a school of thought that new top managers, especially those from outside the firm, typically initiate change and determine the new strategic direction for their organizations (Grimm and Smith, 1991; Miles, Snow, Meyer and Coleman, 1978; Tushman and Romanelli, 1985). The traditional perspective sees the board's role in strategy in these examples as replacing the CEO (Westphal and Fredrickson, 2001). However, as previously discussed, recent research has established that boards are able to influence strategic direction without necessarily resorting to CEO termination (Stiles and Taylor, 2001). Mechanisms such as pressure from institutional investors and other external stakeholders (Useem, Bowman, Myatt and Irvine, 1996; Westphal and Zajac, 1997), the provision of advice from new directors to CEOs (Goodstein and Boeker, 1991; Goodstein *et al*., 1994), social ties between top management and outside directors (Westphal, 1999) and the strategic contexts of board interlocks (Carpenter and Westphal, 2001) have been shown to influence strategic decision making. Furthermore, Westphal and Fredrickson (2001) have demonstrated that boards, particularly under conditions of poor firm performance, formulate strategies that are consistent with the directors' home firm experience and then select a new CEO who has prior experience with the chosen strategy in order to facilitate implementation. In this instance, a powerful board "shapes a firm's strategic direction by selecting a CEO who has experience at implementing the strategy that board members favor" (Westphal and Fredrickson, 2001: 1115). Hence, a more powerful board is more likely to have increased involvement in setting the strategic direction of the company. On this basis we propose that:

> **Proposition 1**: The power of the board in relation to top management is positively related to strategic control and negatively related to financial control by the board.

Our second proposition recognizes the impact of environmental uncertainty on the relative choice of control mechanisms by the board. By drawing on a risk sharing perspective, agency theory argues that, under conditions of low uncertainty, boards will emphasize outcome and hence financial control, by transferring risk to management (Eisenhardt, 1989). However, as uncertainty mounts, management becomes more risk averse and the cost of transferring risk becomes increasingly expensive. In this situation, boards will emphasize behaviour and hence strategic control (Eisenhardt, 1989). Therefore, we propose that:

> **Proposition 2**: Environmental uncertainty will be positively related to strategic control and negatively related to financial control by the board.

Information asymmetry is the third key contingency factor that impacts on a board's relative choice of strategic versus financial control, both from an agency and an organizational control theory perspective (Eisenhardt, 1985, 1989). According to agency theory, under the simple condition of complete information, the principal has full knowledge of the agent's behaviour and a contract based on that behaviour is most efficient (Eisenhardt, 1985). In the case of incomplete information, the principal can either (1) invest in information systems so as to identify the agent's behaviour or (2) contract on the outcomes of the agent's behaviour (Eisenhardt, 1985, 1989) with the choice between these two options resting "upon the trade-off between the cost of measuring behavior and the costs of measuring outcomes and transferring risk to the agent" (Eisenhardt, 1985: 137). According to organizational control theory, the choice of behaviour or outcome control depends on the information characteristics of the given task (Eisenhardt, 1985). High task programmability, also referred to as knowledge of the transformation process, is usually associated with behaviour control (Ouchi, 1979; Thompson, 1967). Given that boards are an "information system for monitoring executive behaviors" (Eisenhardt, 1989: 65), it is reasonable to expect, on the basis of both agency and organizational control theory that increased emphasis on this "information system" aspect is likely to be associated with an increased level of strategic control. Therefore, we propose that:

Proposition 3: Information asymmetry, such as that associated with increasing levels of diversification, will be negatively related to strategic control and positively related to financial control by the board.

The ability of the board to impact on firm performance is a problematic area. Clearly the board can influence strategy. For instance, Carpenter and Westphal (2001) demonstrated that the strategic contexts of board interlocks were an important influence on strategic decision making. Similarly, Westphal and Fredrickson (2001) showed that the strategy experience of directors, not the CEO, was the key factor in influencing diversification decisions in firms with new CEOs. Since decisions such as these will impact on firm performance, we contend that the control mechanism favoured by the board, particularly in light of the firm's contextual requirements, will impact on firm performance. Several scholars have shown that contextual factors have a moderating effect on proxies for the board's strategy role (e.g. Golden and Zajac, 2001; Geletkanycz and Boyd, 2002). Building on this contingency approach, we propose that:

Proposition 4a: The choice of control mechanism by the board will impact on firm performance.

Proposition 4b: Boards that match their emphasis on strategic versus financial control to their strategic context will be associated with positive firm financial performance.

DISCUSSION

We began this paper by noting that the board's role in strategy is commonly presented in the literature as falling somewhere along active-passive continua relative to both formulation and evaluation. We have reviewed the normative and the academic literature and argued that the early managerialist perspective which saw boards as "rubber stamps" has been slowly overtaken by an "active" perspective which sees boards more as independent thinkers who shape the strategic direction of their organizations. We have also outlined three major limitations in the research agenda to date: (1) the lack of an overarching theoretical perspective on the board's strategy role, (2) the reliance on proxies for this role rather than a direct measure, and (3) the lack of quantitative data linking this role to firm financial performance.

In response to these limitations we have developed a new theoretical perspective to explain the board's strategy role. This new approach integrates organizational control and agency theories, arguing that boards exercise a system of financial and strategic controls over top management in a similar manner to those used by corporate managers in diversified firms. Further, we argue that the balance between these control mechanisms depends on the firm's context and provides an indication of the nature and the extent of board involvement in strategy. A critical point to note is that we perceive control as going beyond board constraints on management aimed at reducing self-interested actions. Rather we see control as a broad mechanism to shape strategic direction, and to facilitate innovation and organizational renewal (Stiles and Taylor, 2001).

Previous attempts in the literature to explain the board's strategy role have generally relied on a single theoretical perspective. However, scholars have recently begun to integrate theories in an attempt to explain board roles (Hillman and Dalziel, 2003; Sundaramurthy and Lewis, 2003), arguing that this multiple lens approach "allows for a more fully specified model" and a richer understanding of the relationship between variables such as board capital and the monitoring and access to resources roles (Hillman and Dalziel, 2003: 391). In the same way, we suggest that our integrative approach, by conceiving of board control in such a broad sense, elaborates the board's strategy role and allows for a more in depth understanding of this role and its relationship to firm financial performance. This understanding contributes to knowledge in several ways.

First, it suggests a more parsimonious view of board roles, an area which has received considerable attention but limited agreement in the literature. For example, Mintzberg (1983) proposed seven key roles: selecting the CEO, exercising direct control during periods of crisis, reviewing managerial decisions and performance, co-opting external influences, establishing contacts and raising funds for the organization, enhancing the organization's reputation, and giving advice to the organization. Zahra and Pearce (1989) took a more limited perspective and suggested three roles only: service, strategy and control. Johnson, Daily and Ellstrand (1996) also took a limited perspective and proposed a three role set comprising control, service and resource dependence. Other scholars have also suggested multiple role sets for boards (Hung, 1998; Cravens and Wallace, 2001; Johnson, 1997; Nicholson and Kiel, 2002). While these role sets overlap, there is often a lack of consensus on the functions that make up each role and the terms used to describe these roles. For instance, Zahra and Pearce (1989) saw the "service" role as enhancing company reputation, establishing contacts with the external environment and advising management. Johnson, Daily and Ellstrand (1996) also saw this "service" role as advising senior management, but excluded legitimacy and resource dependence functions in favour of strategy formulation. Nicholson and Kiel (2002) advocated an "advising" role and suggested that strategy and access to resources were separate but related roles. Based on our integrative theory we suggest an alternative conception in which boards only have two key roles: control, of which strategy and monitoring are sub-sets, and access to resources which includes legitimacy and links to other organizations.

Second, in developing the strategic and financial control constructs, our theory provides a platform to study board processes relative to strategy. In this way it addresses the call of scholars such as Pettigrew (1992) and Stiles and Taylor (2001) for more focus on directors' behaviour rather than on board demographics.

Third, the development of strategic and financial control constructs provides an opportunity to address the relationship between board involvement in strategy and firm financial performance. This relationship remains as a major gap in the literature, largely because of the difficulties in measuring the board's strategy role. Just as the development of an adequate measurement model of strategic planning was a major impediment to strategy research generally (Boyd and Reuning-Elliot, 1998) so too is the development of such a model for the strategy role of the board to corporate governance research. By operationalizing strategic and financial control we will be able to develop a direct measurement model for the board's strategy role rather than proxies, one which can then be applied in quantitative studies of firm performance.

Fourth, our model recognizes that the board's relative emphasis on strategic versus financial controls is dependent on contingency factors in the firm's environment. In developing propositions about how board power, environmental uncertainty and information asymmetry affect a board's strategic and financial control, we build on previous empirical studies and provide opportunities for further research.

Finally, our contingency framework suggests four typologies for the board's strategy role according to the extent to which it emphasizes strategic and financial control. This contingency framework has implications for both practitioners and academics. For the former, it suggests that board processes and board/firm context are key considerations in driving firm performance. Similarly, it supports the contention that the distinction between board and management roles in strategy is not clear cut but rather it depends on firm and board context. While our theory does not specifically address director independence, its emphasis on process and context support the notion that prescriptions on independence may not be the "panacea for effectiveness it is thought to be" (Hillman and Dalziel, 2003: 393).

For academics our framework provides a model for further theory development and testing. Theory development could elaborate the likely impact of contingencies such as prior firm performance, institutional ownership and director compensation on the strategy role. Qualitative research is important to clarify the dimensions of the strategic and financial control constructs and could be followed by quantitative studies linking these constructs to accounting or market-based measures of firm performance. Finally, longitudinal studies could be considered to explore how and under what conditions boards change their balance between strategic and financial controls and what impact this has on firm performance.

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Figure 1: Strategic and Financial Control

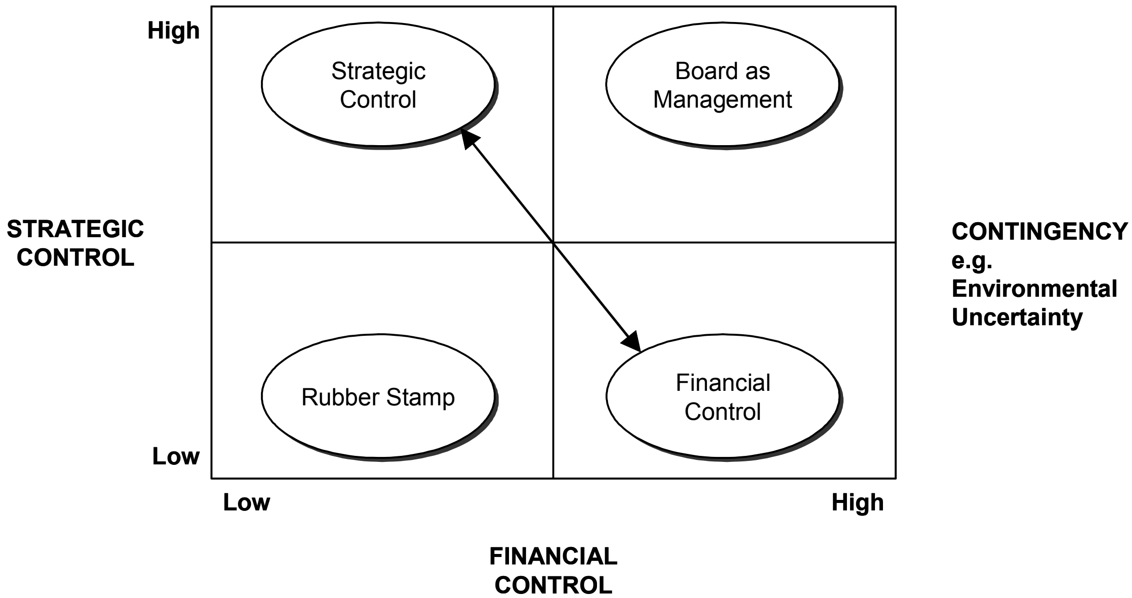

Figure 2: Contingency Factors, Board Strategy Role and Firm Performance

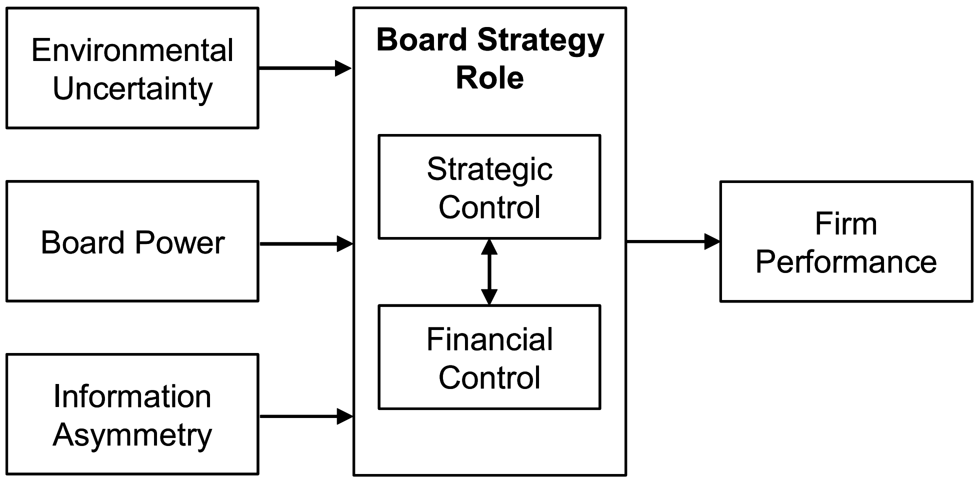

Table 1: Levels of Part-Time Board Member Involvement in Strategy

	Taking Strategic Decisions	Shaping Strategic Decisions	Shaping the Content, Context and Conduct of Strategy
Definition	Influence is exerted inside the boardroom at the end of the capital investment decision process	Influence occurs early in the decision process as part-time board members shape the preparation of capital investment proposals by executives	Influence is continuous and not confined to decision episodes
Board Behaviour	Inside the boardroom, boards take decisions to either accept, reject or refer capital investment proposals	Consultation with part-time board members by the executive, either formally or informally, whilst a capital investment proposal is being prepared enables board members to test ideas, raise issues, question assumptions, advise caution, and offer encouragement. Executives 'sieve' capital investment proposals in anticipation of the need for board approval	The board develops the context for strategic debate, establishes a methodology for strategy development, monitors strategy content and alters the conduct of the executive in relation to strategy
Board Involvement	All boards take strategic decisions	Some boards shape strategic decisions	A minority of boards shape the context, content and conduct of strategy

Source: McNulty and Pettigrew, 1999: 55