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ARTICLE

The roles played by boards of directors: an integration of the agency and stakeholder theories

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ABSTRACT
This paper explores the development and articulation of the agency and stakeholder theories of the firm and their corresponding logics of shareholder wealth maximisation and stakeholder interest optimisation. We note how these two perspectives have been viewed as diametrically opposite normative, instrumental and descriptive theories, despite efforts by some authors to find common ground. Each has served as a basis for firm governance. We explore the relationship of the agency and stakeholder theories to the conceptualisations of the roles of boards of directors, and how both theories hold value in understanding two board functions/roles: control/monitoring roles and service roles (which covers both resources and strategy).

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For decades, a value-laden debate has raged about the over-riding corporate objective (Sundaram & Inkpen, 2004): shareholder wealth maximisation or wider stakeholder benefit. Interestingly, the two most strikingly distinct and, to some extent, dominant theoretical manifestations of this debate emerged in relative concurrence: agency theory as a description of how the firm will set about to ensure stakeholder interests are protected in light of the separate of ownership and management functions (Jensen & Meckling, 1976), and stakeholder theory as a descriptive and fundamentally normative explanation for management focus on a wider range of stakeholders interested in the firm (Friedman, 1984).

At their centres, each of these theoretical perspectives is about governance. They provide a basis for understanding how decisions are made by those within the firm – be they managers, owners or stakeholders. Governance has been defined as 'the determination of the broad uses to which organisational resources will be deployed and the resolutions of conflicts among the myriad of participants in organisations' (Daily, Dalton, & Cannella, 2003). As boards of directors play a critical role in these determinations (Pye & Pettigrew, 2005), this paper seeks to explore agency and stakeholder theories from the perspective of the key roles of board of directors.

We begin this exploration with an extensive review of both agency and stakeholder theories, covering the criticisms of each and where they coincide and differ. This is followed by an exploration of the key roles of boards of directors as set out in the literature. We then look at how agency and stakeholder theories contribute to our understandings of these roles. Finally, we conclude that both agency and stakeholder theories contribute to the understanding of how boards function and how boards fulfil their roles of control/monitoring and service, and to theorising about how their execution of the governance function can best be fulfilled.

Agency and stakeholder theories

First: Agency theory

Stimulated by perspectives on the behavioural implications of property rights and the work of Coase (1937), agency theory, as expressed by Jensen and Meckling (1976), has been described by a truly remarkable spectrum of academics as the dominant theory of the firm and corporate governance (Daily et al., 2003; Kacperczyk, 2009; Carney, Gedajlovic, & Sur, 2011; Hill & Jones, 1992, Kochan & Rubinstein, 2000). Jensen and Meckling (1976) proposed agency theory to generally explain the existence and functioning of the public corporation (the preference

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of internal organisation over market based contracts because of the greater availability and efficiency of control instruments (Williamson, 1971)), and to specifically highlight the dominant corporate form; wherein ownership and management functions are separated despite the possibility for the divergence of interests.

The core of agency theory is the principal–agent relationship, wherein one person (the principal) engages another (the agent) to perform a service on their behalf involving decision-making authority. With its origins in economic theory (Williamson, 1971), agency theory's critical assumption is that, all-else-being-equal, any individual will act in their own self-interest (Eisenhardt, 1989; Hill & Jones, 1992; Shankman, 1999). In the context of the firm, managers are assumed to be inclined to act in their own self-interest (note, this is not particular to managers but rather an *a priori* assumption about all individuals), and there will be times when these interests may not align with those of the owners of the firm (e.g. managers may be more risk averse than owners because they are not able to diversify risk by virtue of their level of financial dependence on the firm). Hill and Jones (1992) describe this as the 'cornerstone' of agency theory (p. 132). Carney et al. (2011) describe this as a conflict, for

> professional managers with little or no ownership stake in the firms they manage make decisions on behalf of shareholders, but have little incentive to manage the firms efficiently or in a manner consistent with the interests of its shareholders. (p. 485)

According to Jensen and Meckling (1976), owners/principals can limit the impact of this divergence of interest through monitoring and control of the behaviours and actions of the agent. Monitoring may take the form of measuring and observing the behaviour of the agent; while examples of control mechanisms include budgets, rules and policies, and incentives. However, these mechanisms themselves bring costs to the firm, such that their use involves a trade-off between the risks and costs of divergent behaviour and the risks and costs of monitoring and control. Such monitoring costs and bonding costs (e.g. reporting) that the principal will direct the agent to incur to ensure that the latter does not take certain actions, will nevertheless not prevent the agent from still taking some actions that diverge from the interests of the principal. This final cost of divergent action represents residual loss. The combination of these monitoring costs, bonding costs and residual loss represent the agency costs of the corporation (Eisenhardt, 1989).

Fama and Jensen (1983) and Eisenhardt (1989) extensively build on the work of Meckling and Jensen (1976) to further set out agency theory as a theory of the firm by: (1) noting that separation of ownership and management is an efficient specialisation of function; (2) identifying that natural selection will favour the firm that minimises the economic costs of agency; and (3) exploring governance structures that will be most efficient for this minimisation. These structures provide mechanisms to police explicit and implicit contracts between principals and agents and will include laws, key monitoring mechanisms (particularly boards of directors), and enforcement mechanisms (such as laws, policies, contracts and incentives).

Eisenhardt (1989) and Rutherford, Buchholtz, and Brown (2007) explicate in greater detail the specific problems arising from the separation of interests between the owner (principal) and the manager (agent). Moral hazard relates to the potential for the manager to act opportunistically (e.g. pay exorbitant salaries to themselves or neglect their duties), while adverse selection refers to the inability of owners to verify the information agents provide (e.g. information about their skills during the hiring process). These potential acts reflect the fact that owners and managers have different goals (i.e. owners prefer actions that maximise return on investment in the firm while managers prefer actions that maximise their own personal outcomes) and the asymmetry of information between owners and managers (wherein the owner cannot confirm that the manager is acting in the best interests of the owner). Eisenhardt (1989) fittingly summarises that agency theory is grounded in the divergence of principal and agent interests, and that it is difficult or expensive for the principal to know what the agent is doing and to influence this behaviour. This is an information problem which, from an instrumental perspective, will impact what mechanism of contract is best chosen in efforts to most efficiently align agent behaviour (given moral hazard and adverse selection) with principal interests. Where the outcome in the interest of the principal is easy to measure, an outcome-based contract will best ensure that the actions of the agent will be aligned with the principal's interest. Such a contract is therefore economically optimal in such a situation. In contrast, in situations where it is more difficult to define and measure the achievement of the outcome desired by the principal, it may be more economically efficient to focus on the measurement and control of the behaviours of the agent. Both outcome and behaviour/control-based contracts are employed as mechanisms to reduce agency costs in relation to the availability and reliability of information and the degree of information asymmetry between principal and agent. The key components of agency theory, as summarised by Eisenhardt (1989), are adapted in Table 1.

Table 1. An overview of agency theory adapted from Eisenhardt (1989).

Key idea	Principal–agent relationships should reflect efficient organisation of information and risk-bearing costs
Unit of analysis	Contract between principal and agent
Human assumptions	Self interest Bounded rationality Risk aversion
Organisational assumptions	Partial goal conflict among participants Efficiency as the effectiveness criterion Information asymmetry between principal and agent
Information assumptions	Information as purchasable commodity
Contracting problems	Agency (moral hazard and adverse selection) Risk sharing
Problem domain	Relationships in which the principal and agent have partly differing goals and risk preferences (e.g. compensation, regulation, leadership , impression management, whistle-blowing, vertical integration, transfer pricing)

Fama and Jensen (1983) and Eisenhardt (1989) also introduce the notion of risk – building on Jensen and Meckling (1976) – as a further factor of agency theory. As agents and principals have different interests, they will also have different risk preferences. Economic models assume owners and shareholders are assumed to be wealth-maximisers who will seek to maximise efficiency of the organisation. Owners and shareholders are relatively risk positive as they have the ability to diversify their economic investments, whereas manager/agents cannot diversify their investment in the firm and therefore are relatively risk adverse. In contrast to the tendency or owner/shareholders to maximise wealth, managers are inclined to take actions that maximise growth in order to maximise remuneration, power, job security and status (all shown to be functions of organisational size) (Hill & Jones, 1992).

Thus, agency theory serves a descriptive role in explaining the emergence of the corporate organisational form and an instrumental role in providing positive propositions about efficient contracting mechanisms to minimise agency costs (Eisenhardt, 1989; Fama & Jensen, 1983; Jensen & Meckling, 1976). However, it has also been applied normatively as the 'shareholder value' view of the corporation that singularly describes the purpose as the maximisation of shareholder value (Carney et al., 2011; Kacperczyk, 2009; Shankman, 1999). The underlying assumption, normatively interpreted as the 'way it is,' is that the goal of owners is to maximise net-present-value of the firm and agents should act in a manner to achieve this goal. Agency theory is then applied instrumentally in service of that goal (Eisenhardt, 1989; Heath & Norman, 2004; Shankman, 1999; Sundaram & Inkpen, 2004). This has led to research into the mechanisms by which boards of directors seek to solve the problems of divergence of manager interests from those of the owner shareholder. Exploration has centred on two key mechanisms: (1) boards using monitoring to enhance owner information (Eisenhardt, 1989; Johansen, 2008); and (2) the use of controls, particularly incentives. While some research have considered the implementation of rules and policies to limit decision making authority (Michael & Pearce, 2004), most of the conducted research has been concerned with the use of executive compensation contracts to address managerial incentives (Beatty & Zajac, 1994; Carney et al., 2011; Daily et al., 2003; Eisenhardt, 1989). Of particular importance is the observation by Beatty and Zajac (1994) that the risk bearing concerns associated with contingency pay (i.e. managers are asked to bear the risk associated with firm performance in environments where their ability to impact performance may be constrained and where they are unable to diversify their personal risk) may lead boards of directors to address the problem through board structure to ensure monitoring. Carney et al. (2011) support this view, noting that 'the tension between shareholders and managers over value allocation has lately shifted away from the design of incentives toward the intensification of monitoring and accountability' (Carney et al., 2011). Dalton, Daily, Ellstrand, and Johnson (1998), in a meta-analysis, found no support for the speculated relationship between board structure and performance.

Criticisms of agency theory

Despite the dominance of agency theory as a theory of the firm, it has also been subject to extensive criticism (Carney et al., 2011; Eisenhardt, 1989; Perrow 1986; Shankman, 1999). Two of these stand out in particular: (1) that it is overly narrow in its focus, and (2) that it is devoid of moral standing. First, agency theory is criticised for overly and narrowly focussing on the tension between owners and managers, at the expense of attention to numerous other tensions within the firm (e.g. minority and controlling investors, senior and new employees, and

insiders and arm's length buyers) (Carney et al., 2011). Critics argue that the theory ignores these tensions in focussing on manager/agent attention to the interests of the shareholder/principle above all else (Shankman, 2011). This narrow view neglects the diversity of contractual and non-contractual interactions that impact the modern corporation, particularly in a globalised world (Donaldson & Preston, 1995; Hill & Jones, 1992). In many ways, it ties directly back to the simple input–output model of the firm, and hence represents a narrow conceptualisation. Secondly, while the criticism of agency theory as narrow focuses on its descriptive and instrumental utility (Donaldson & Preston, 1995), it is even more roundly critiqued on normative grounds. As Carney et al. (2011) write, the heart of agency theory is the normative acceptance of shareholder value maximisation and the self-interested behaviour of agents. This view is anchored in the economic literature (Coase, 1937, Williamson, 1971) and sees any action or activity from the perspective of the economic benefit to the firm and as the product of a series of contracts. In doing so, the theory neglects or denies any contention that the agency relationship (like any other human relationship) is constrained by moral principles (which may actually be defined and derived from the market itself – e.g. honouring agreements, avoiding lying, respecting autonomy of others, and avoiding harm to others (Shankman, 1999). Perrow (1986) is most harsh in this criticism, describing agency theory as 'dangerous' and 'insidious.'

Second: Stakeholder theory

In 1970, Friedman published his iconic paper 'The social responsibility of business is to increase its profits' in which he held how a firm's main responsibility is to maximise the returns for its shareholders and that a company has no social responsibility to the public or society. Friedman's doctrine (i.e. shareholder theory) would be later criticised for its lack of support for Corporate Social Responsibility (CSR) and for not taking into account all the interests of the different firm stakeholders. Consequently, against this perceived dominance of the shareholder-centric view of the firm, and the corresponding utility and taken-for-granted nature of agency theory, stakeholder theory emerged as a seemingly alternative response (Donaldson & Preston, 1995; Hill & Jones, 1992; Kochan & Rubinstein, 2000; Mainardes, Alves, & Raposo, 2011). Most influentially set out by Freeman (1984), stakeholder theory emerged to highlight and advocate the strategic importance of groups other than just the shareholder, including not only the suppliers, employees and clients, but also the local community, environmental groups, governments and even competitors (Mainardes et al., 2011). In explicating stakeholder theory, it is most informative to first consider it as a descriptive tool to understand the workings of the firm (Donaldson & Preston, 1995). Where the traditional view of the firm considered basic input (suppliers, investors/shareholders and employees) and output (customers) flows, the stakeholder model instead describes two-way flows between the firm and a multitude of stakeholders, wherein none of the stakeholders is necessarily more important than any other. Critically, the hegemony of the shareholder is both descriptively challenged and normatively denied (Donaldson & Preston, 1995; Hill & Jones, 1992; Mainardes et al., 2011). Each of these groups is held to have a potentially legitimate interest in participating in an enterprise to obtain benefits, and no interest is held to be automatically paramount over another. Of note, but beyond the scope of this review, is the challenge experienced in the literature in developing a commonly accepted definition of stakeholder (see Mitchell, Agle, & Wood, 1997).

It is important to note that the emergence of the stakeholder view and theory of the firm coincided with articulation of the resource dependence theory of strategic management of the firm (Pfeffer & Salancik, 1978). Resource dependence theory was developed by Pfeffer and Salancik (1978) to understand the influence of external factors on organisational behaviour, wherein organisations will attempt to reduce the power of others over them and to increase their own power over others. They do this by taking actions to manage their external interdependencies with a goal of seeking power that will enable strategic advantage. In this context, there is obvious overlap with the resource-based view of strategy, wherein firms will seek sustainable competitive advantage through the exploitation of rare, inimitable, and valuable resources (Hillman, Withers, & Collins, 2009).

As reported in Mainardes et al. (2011), the basic premises of stakeholder theory as described by others (Jones & Wicks, 1999; Mainardes et al., 2011; Savage, Dunkin, & Ford, 2004) are:

- the organisation enters into relationships with many groups that influence or are influenced by the company, i.e. 'stakeholders' in accordance with Freeman's terminology;

- the theory focuses on the nature of these relationships in terms of processes and results for the company and for stakeholders;
- the interests of all legitimate stakeholders are of intrinsic value and it is assumed that there is no single prevailing set of interests, as Clarkson (1995) and Donaldson and Preston (1995) pointed out;
- the theory focuses upon management decision making;
- the theory explains how stakeholders try and influence organisational decision-making processes so as to be consistent with their needs and priorities; and
- organisations should attempt to understand and balance the interests of the various participants.

Donaldson and Preston (1995) explained the resonance of stakeholder theory on the grounds of its descriptive accuracy, instrumental power and normative validity. To them, the theory:

> describes the corporation as a constellation of cooperative and competitive interests possessing intrinsic value … [it] establishes a framework for examining the connections, if any, between the practice of stakeholder management and the achievement of various corporate performance goals … [and] its fundamental basis is **normative** and involves acceptance of the following ideas: (a) stakeholders are persons or groups with legitimate interests in procedural and/or substantive aspects of corporate activity. Stakeholders are identified by their interests in the corporation, whether the corporate has any corresponding functional interest in **them**. (b) The interests of all stakeholders are of **intrinsic value**. (pp. 66–67).

As set out in Sundaram and Inkpen (2004), extensive attempts have been made to link stakeholder management with firm performance. Claims are made of the positive effects of stakeholder management on long-term firm success, on competitive advantage, and on management (Donaldson & Preston, 1995; Mitchell et al., 1997; Hill & Jones, 1992). However, as noted most clearly in Carney et al. (2011), empirical support for these views are 'mixed' (p. 487).

Criticisms of stakeholder theory

Not surprisingly, many of the criticisms of stakeholder theory are in fact counterpoints to the criticisms of agency theory. Where agency theory is viewed as too narrow and focussed, stakeholder theory is criticised as too broad. Not only has the literature failed to settle on a common definition of stakeholder (Mitchell et al., 1997), but Freeman's (1984) work has also been criticised as failing to distinguish between various stakeholders and their relative importance to the firm (Donaldson & Preston, 1995; Hill & Jones, 1992). In its breadth, stakeholder theory is criticised for being imprecise in both its descriptive capacity and in its instrumental utility. Sundaram and Inkpen (2004) set this out in detail, highlighting the following points:

- By suggesting that managers have more than one objective function (by virtue of seeking to satisfy multiple stakeholders as opposed to the shareholder), stakeholder theory creates a recipe for confusion and inefficient decision making.
- Stakeholder attention distorts risk-taking by managers, as stakeholders, such as employees, suppliers and communities, will have incentives to dissuade managers from risk-taking activities.
- The evidence for a focus on stakeholder management leading to firm performance is weak, wherein the goal of maximising shareholder value is pro-stakeholder in that it generates the economic performance that benefits the primary stakeholder in the long run (Carney et al., 2011).

The most common criticism of stakeholder theory comes in response to the normative dimension; just as agency theory is said to be devoid of a moral basis, stakeholder theory is said by some to be entirely normative (Carney et al., 2011; Kacperczyk, 2009; Sundaram & Inkpen, 2004). Wherein the economic view of the firm has an instrumental basis, the stakeholder view often drives back to moral-ethical foundations (Shankman, 1999). This plays out in the assumptions of stakeholder theory about individual motives (enlightened self-interest) and behaviour (contingent and morally driven) and the very nature of relationships (contingent as opposed to divergent) (Shankman, 1999). Stakeholder theory can appear, and may in fact be rightly described as, a

Table 2. Comparing the dimensions of agency and stakeholder theories, adapted from Shankman (1999) and Carney et al. (2011).

Dimension	Agency theory	Stakeholder theory
Purpose of the firm	Shareholder wealth maximisation	Locus for wider external stakeholder interests
Theoretical underpinnings	Transaction cost economics	System theory
Explanatory power	Narrow	Broad
Level of analysis	Individual	Individual/firm/societal
Unit of analysis	contract	Interests/relationships
Direction of relationships	One-way	Two-way
Assumption of human behaviour	Bounded rationality Risk aversion Opportunistic Adverse selection	Bounded rationality Risk aversion Contingent
Motive	Psychological egoism Rational preference seekers	Enlightened self-interest Economic and social
Normative	No	Yes
Nature of market	Perfect	Imperfect
Criteria for organisational effectiveness	Efficiency	Fairness
Governance focus	Mitigating agency cost Minimising transaction cost	Identifying and resolving stakeholder concerns
Governance mechanism	Managerial monitoring Alignment of incentives	Network: control embedded in lasting relationships
Implication for practice	Align interests of employees and owners: take actions insofar as they maximise firm NPV: use efficient contracting mechanisms to minimise agency cost	Balance in equilibrium the interests or claims of all relevant stakeholders.

counter-balancing response to the amoral economic view of the firm (Mainardes et al., 2011). As Mainardes et al. (2011), write:

> [Stakeholder theory orients] its principles towards the application of theory as a proposed relationship between the company and its stakeholders within a fair, ethical and morally correct framework (deontological principles) where interests are not purely economic (utilitarian principles), thereby justifying both the actions of management as well as the results obtained. (p. 233)

Sundaram and Inkpen (2004) label this as clearly naïve.

Third: Reconciling agency and stakeholder views

As seemingly opposite yet relatively equally dominant views/theories of the firm, agency and stakeholder theories have been logical subjects for explorations of similarities and differences (Carney et al., 2011; Hill & Jones, 1992; Quinn & Jones, 1995; Shankman, 2011). Table 2 summarises this comparative analysis.

Viewed in this manner, it is possible, and even tempting, to continue to view agency and stakeholder views of the firm and the corresponding theories as opposing and irreconcilable theories. However, Hill and Jones (1992) see them as possibly complementary and, consequently, develop a 'stakeholder-agency theory' which describes the firm as a nexus of contracts between resource holders, not only shareholders but also other stakeholders with valuable resources required by the firm (a la resource dependence theory). As such, implicit and explicit contracts (as per agency theory) are understood to define and guide management and firm action in relation to all stakeholders (as per stakeholder theory). Similarly, Carney et al. (2011) focus on intra-stakeholder and inter-stakeholder conflicts and tensions within particular governance systems. Whereas key components of agency theory have been focussed on the managerial-ownership conflict, the authors apply these components to the wider range of conflicts. In doing so, they suggest that authority structures (e.g. managerial, stakeholder and family) will have differential effects on the mechanisms for addressing these inherent stakeholder conflicts. The result is an integration of agency theory and stakeholder theory in the interests of greater descriptive and instrumental power.

In contrast to Hill and Jones (1992) and Carney et al. (2011), Sundaram and Inkpen (2004) consider whether stakeholder theory provides a viable alternative to agency theory and its focus on shareholder value maximisation. Their instrumental and normative conclusion is that shareholder value should be the preferred corporate goal for five reasons:

1. The goal of maximising shareholder value is pro-stakeholder.
2. Maximising shareholder value creates the appropriate incentives for managers to assume entrepreneurial risks.

3. Having more than one objective function will make governing difficult, if not impossible.
4. It is easier to make shareholders out of stakeholders than vice versa.
5. In the event of a breach of contract or trust, stakeholders, compared with shareholders, have protection (or can seek remedies) through contracts and the legal system (Sundaram & Inkpen, 2004, p. 353).

To sum up, the review of the literature as outlined above shows continual conflict between agency and stakeholder views of the firm. However, it also shows that some integration and reconciliation is possible – perhaps from a normative perspective, and certainly from descriptive and instrumental viewpoints. It is with this recognition that we first consider the roles of boards of directors in governance and then explore the contributions and reconciliation of agency and stakeholder views.

Boards of directors

The advent of the 21st century reflected a metamorphosis in the roles played by boards of directors (BOD), and how their responsibilities have come to include not only reflecting shareholders' interests, but also addressing stakeholders' needs and 'going into the real world and tackling the emerging concerns regarding social and ecological practices' (Chams & García-Blandón, 2019b, p. 1067). One of the reasons behind such transformation is the collapse of the global financial markets of 2008–2009 (Kemper & Martin, 2010). Another reason is the increasing dependence on business technology (e.g. mobile and cloud technologies, social media, and big data) (Valentine & Glenn, 2013) which has led to the BOD's need to show their Enterprise Business Technology Governance (EBTG) leadership capability (Valentine & Glenn, 2015). Different studies have demonstrated that the BOD structure has become a key catalyst to social and ecological achievements (Lawrence, Collins, & Roper, 2013; Post, Rahman, & Rubow, 2011) and it now influences both financial and non-financial objectives (Galbreath, 2018). For example, board members have become contributors to various societal activities, such as encouraging ethical and moral engagement, philanthropic influences, implementation of ethical codes, compliance with laws and policies, awareness of environmental concerns, social disclosures reporting, and stock market indicators (El-Kassar, Messarra, & Elgammal, 2015). This connection between BOD and sustainable practices (e.g. environmental, social, and governance (ESG); corporate social responsibility (CSR); triple bottom line (TBL); and corporate or business sustainability (Chams & García-Blandón, 2019a)) can be emphasised through both the agency view (which focuses on the board's mechanism to be structured and designed in a way that implements social and ethical performances, with the latter having some efficient benefits and promising returns (McWilliams & Siegel, 2000)) and the stakeholder view (which embraces a broader societal embeddedness of organisations and their interdependencies with the societal environment, postulating that 'the purpose of business is to create value for all stakeholders' (Hörisch, Freeman, & Schaltegger, 2014, p. 331)).

Roles of boards

While there are numerous different frameworks that one can use when setting out the roles of boards of directors (for example, see Chait, Ryan, and Taylor (2005) for an explication of fiduciary, strategic and generative thinking), at the highest level, it is possible to be quite succinct. With a perspective shared by others, Forbes and Milliken (1999) suggest that only two key roles, control and service, are necessary to understand boards (see also Daily et al., 2003; Hillman & Dalziel, 2003).

Control/monitoring role

The control role of the board relates to the monitoring of management on behalf of the shareholders (or other owners on stakeholders in business forms other than the for-profit corporation). It encompasses general legal duties for loyalty and care, and specific duties such as the hiring, compensation and replacement of senior managers and oversight of their activities (Daily et al., 2003; Forbes & Milliken, 1999). It also encompasses the ratification – for example of financial accounts – of management decisions and actions (Johanson, 2008). As such, boards have been characterised as the 'apex of the firm's decision control system' (Forbes & Milliken, 1999, p. 491). It is within this context that the distinction is generally made between the role of the board to monitor

and ratify and the role of management to initiate and implement (Johanson, 2008; Payne, Benson, & Finegold, 2009).

Service role

Boards are also felt to have roles beyond the relatively distinct function (defined here in the singular) of monitoring and control. Daily et al. (2003) point to resource (i.e. providing access to resources needed by the firm), service (i.e. providing advice and counsel to the firm's management) and strategy (i.e. generating and analysing strategic alternatives) roles for the board. The perspective that these three roles are distinct, or that the strategy role is distinct from a resource/service role, has occupied a significant portion of the literature (Daily et al., 2003; Hillman & Dalziel, 2003; Pugliese et al., 2009). As such, it is appropriate to briefly set out the arguments expressed as to the appropriateness of such a distinction.

We share the view of Hillman and Dalziel (2003) and Forbes and Milliken (1999) that the service role encompasses resource and strategy roles. The resource role for the board refers to the function of the board (as individuals and as a collective) to bring to the organisation resources that might not otherwise be available. This can be in the form of expertise, experience and skill, but it can also be in the form of access to external resources through the connections or abilities of the director or directors. This can be enabled via the experience of the director (e.g. their 'day-job'), but it can also be enabled through their social network (e.g. interlocking directorates). However, at its core, the role of the board in bringing or enabling access to external resources to the firm is a service role which is not distinct from any other advice, counsel or activity that the directors provide to management. In sum, it is appropriate to view the service function as one of directors bringing resources (be they the director's own talents, advice or counsel or be they external resources to which the director facilitates access) to the firm to supplement those available to management (Hillman & Dalziel, 2003; Forbes & Milliken, 1999). A similar question emerges when one considers the extent to which it is necessary to distinguish the strategy role from that of service (which we argue encompasses the resource role). As Pugliese et al. (2009) note, the board's involvement in a strategic role has been widely debated (Daily et al., 2003; Zahra & Pearce, 1989). This can be traced to Fama and Jensen (1983) distinction between decision management (i.e. initiating and implementing strategic decisions) and decision control (i.e. ratifying and monitoring strategic actions), wherein the roles of management in the former and boards in the latter are distinctly separated. This in turn is consistent with views that boards are distant from day-to-day operations, have information asymmetries with management, and require independence to fulfil the control/monitoring roles (Pugliese et al., 2009). Westphal and Fredrickson (2001) argue that boards have little independent influence over strategic direction (i.e. they provide information and expertise but not strategy) except to the extent that they bring strategies that align with their home firm. Nevertheless, whatever the boundary is with respect to the question of role in strategy, we argue that it is not only parsimonious but appropriate to view this as another form of service, which is contrary to the views of Kim Burns, and Prescott (2009) who argue that there is a distinction. We believe that whether the board is merely commenting upon strategies formulated by management (i.e. analysis) or is an active participant in their development (i.e. generating), it is still appropriate to view this as an expression of the service role. Thus, as argued by Hillman and Dalziel (2003), it is appropriate to consider the general roles of the board of directors for our purposes to be viewed as ones of control/monitoring and service. In general, Pugliese et al. (2009) note that boards are in an excellent position to contribute to strategic decision making by facilitating and empowering managers through the provision of access to service and resources, upon which the firm depends. This is strategy as service.

To sum up, the board of directors plays two major roles: control/monitoring and service (which encompasses both resources and strategy). The next sections discuss how and to what extent both the agency and stakeholder theories explain those roles (Figure 1).

Agency theory and boards of directors

Control/monitoring role

Fama and Jensen (1983), Eisenhardt (1989) and others (Dalton et al., 1999; Zahra & Pearce, 1989, Zahra 2007) developed the role of boards in relation to agency theory wherein the board acts as the primary mechanism to ensure that management is serving the best interests of the owners of the company (through the use of control/monitoring) (Payne et al., 2009). Agency theory provides an extremely clear, concise and simple explanatory

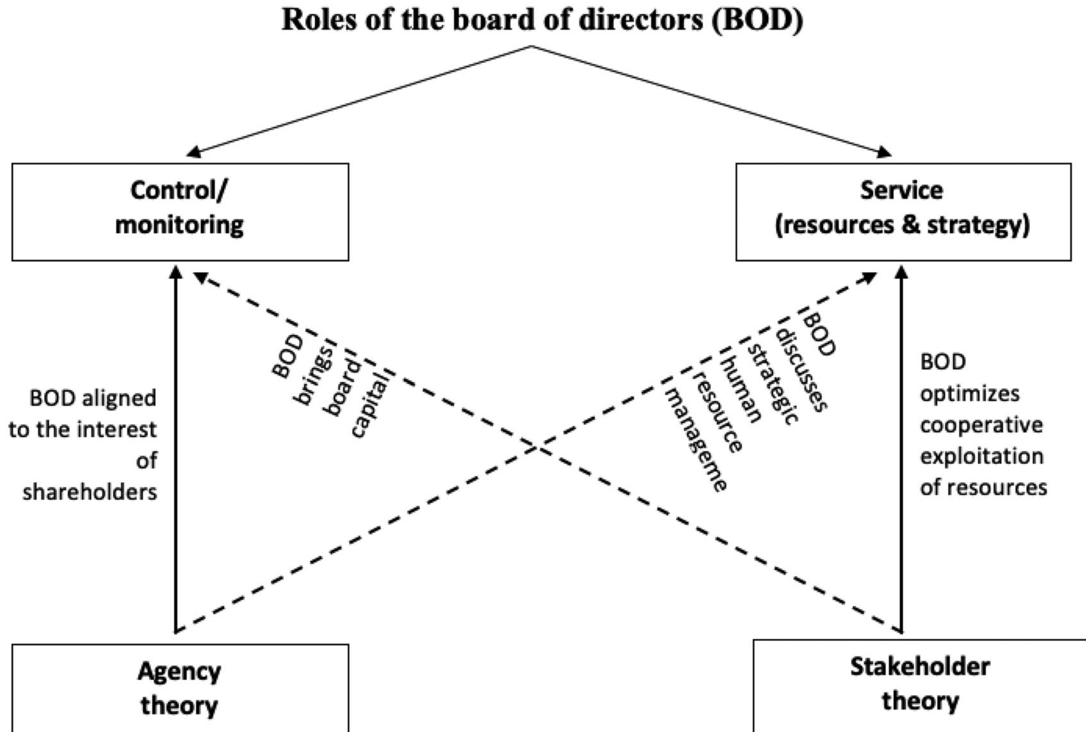

Figure 1. The roles of the board of directors as explained by agency and stakeholder theories.

rationale for the control/monitoring role of the board of directors (Daily et al., 2003). The interests of managers and owners diverge, for managers will be inclined to act opportunistically. As a result, corporate governance mechanisms must focus on ensuring that the actions of managers, and therefore corporate outcomes, are aligned with shareholder interests. The boards of directors exist as the primary mechanism for achieving that assurance through the use of monitoring and controls (particularly incentives).

Boards of directors, bearing the primary responsibility for dealing with these problems, have two solutions available to them: increasing monitoring to improve the information they possess and the use of controls (particularly incentives). While some research has focussed on mechanisms for boards to improve their information (Eisenhardt, 1989; Johansen, 2008), the majority of research has concentrated in the area of controls. And while some of this has considered the implementation of rules and policies to limit decision making authority (Michael & Pearce, 2004), the vast majority has focussed on the use of executive compensation contracts to address managerial incentives (Beatty & Zajac, 1994; Daily et al., 2003; Eisenhardt, 1989). Of particular importance is the observation by Beatty and Zajac (1994) that the risk bearing concerns associated with contingency pay (i.e. managers are asked to bear the risk associated with firm performance in environments where their ability to impact performance may be constrained and they are unable to diversify their personal risk) may lead boards of directors to address the problem through board structure to ensure monitoring. Dalton et al. (1998), in a meta-analysis, found no support for the speculated relationship between board structure and performance.

Despite the absence of empirical clarity as to the effectiveness and mechanisms of board control and monitoring functions, agency theory remains the prevailing explanatory construct. It is also relevant to highlight the contrasting options for controls; assessment of outcomes or behaviours. Whereas outcomes can be subject to significant external risk, uncertainty and time delay, and therefore, be associated with contract premiums, the monitoring of behaviours can be particularly costly. Agency theory helps to explicate the challenge of such contracts (Golden & Zajac, 2001).

Stakeholder theory and boards of directors

Service role

Where agency theory is the prevailing mechanism to explain and explore the monitoring/control role of the board of directors, stakeholder theory provides a compelling focus for understanding the service role.

Where agency theory is about a conflict perspective (i.e. managers are self-interested agents that require monitoring), stakeholder theory, and its close cousin resource dependence theory, is about a consensus perspective where board members are conceived of as part of a wealth creating team where they act as impartial corporate coordinators between stakeholders and are in an excellent position to contribute to the firm by providing access to resources (Kaufman & Englander, 2005).

Stakeholder theory helps to understand the influence of external factors on organisational behaviour, as in resource dependence theory wherein organisations will attempt to reduce the power of others over them and to increase their own power over others. They do this by taking actions to manage their external interdependencies with a goal of seeking power that will enable strategic advantage. Again, the theoretical application of resource dependence theory and stakeholders to the role of the board is both simple and powerful. Boards of directors enable firms to reduce their dependence on the external environment and to gain outside resources. Hence, boards and board members serve to bring external resources for the benefit of the firm (Payne et al., 2009). They serve as boundary spanners of the organisation and the environment (Daily et al., 2003), and serve the organisation through four mechanisms:

> (a) information in the form of advice and counsel, (b) access to channels of information between the firm and environmental contingencies, (c) preferential access to resources, and (d) legitimacy. (Hillman et al., 2009, p. 1408–1409)

Boards also assist managers in better understanding and addressing the needs, and the opportunities for value exchange, of other stakeholders (Kaufman & Englander, 2005).

For example, advice and counsel can take the form of legal advice provided by lawyers sitting on the board or political advice from ex-politicians. Access to channels of information between the firm and the environment can take the form of exploitation of the business connections of individual directors, often achieved through interlocking directorships which ensure that boards have a greater awareness of the environment of partners (and even competitors) than might otherwise be possible. Preferential access to resources has been explored in relation to the extent that directors who are executives of financial institutions may assist in securing external financial support (Daily et al., 2003). Finally, the legitimacy provided by particularly qualified and well-known directors can increase firm reputation. Consistent with our earlier view, each of these mechanisms exists as a general 'service' to the firm provided by directors.

A particularly interesting theoretical construct which has been developed to capture the magnitude and mechanisms of these service benefits is that of board social capital (Hillman & Dalziel, 2003; Tian, Haleblian, & Rajagopalan, 2011). Board capital is the human capital, in the form of the individual experience, expertise and interests, and the social capital, in the form of access to useful information and resources through experiences and connections, that the director brings to the firm (Tian et al., 2011). Greater levels of board capital enable the board to understand and address the needs of stakeholders, secure more resources and more effectively monitor the company, and as such may serve as a linking mechanism between agency and stakeholder theories and between control/monitoring and service functions (Daily et al., 2003; Hillman & Dalziel, 2003). As Kaufman and Englander (2005) write:

> stakeholder theory … argues that boards should have both a monitoring and a consultation function. Boards should be comprised of diverse members, each of whom brings important resources, to compose a board capable of assisting the firm to create and sustain competitive advantage. (p. 12)

Applying agency and stakeholder theories to the control/monitoring role of the board

The control/monitoring role of the board of directors has seen extensive exploration in the context of the relationship and interaction between the board and the chief executive officer (Eisenhardt, 1989; Daily et al., 2003; Dalton et al., 1998). In particular, this literature has focussed on the matter of CEO compensation as viewed from an agency perspective; exploring such matters as the impact of board composition and size on the use of incentives in CEO pay (Daily et al., 2003; Dalton et al., 1998). Notably, the extent to which board composition (in the form of a greater balance of directors who are independent from management as suggested in agency theory) impacts the financial performance of the firm, through the vehicle of incentives to better align CEO interest with those of the firm, has not been empirically demonstrated (Dalton et al., 1998; Daily et al., 2003). Similarly, there is

an absence of research about what information boards of directors have access to and how they use that information (Johanson, 2008).

While there is extensive literature on CEO compensation as a particular reflection of the intersection of the board monitoring/control role and agency theory, there also exists extensive research exploring the relationship between firm performance and the presence of outside directors who are presumed to be better able to exercise the monitoring and control function on behalf of owners as per agency theory (Daily et al., 2003). This line of reasoning leads to the proposition, from an agency perspective as it relates to the board's role in control/monitoring, that independent boards will be better able to align the actions of management with the interests of the firm. This is primarily exercised in the form of independent directors aligned to the interests of shareholders.

It is also possible to identify opportunities for exploring the intersection of stakeholder theory, and the control/monitoring role of the board. This rests extensively on what has been termed board capital, namely the extent to which directors bring skills and experiences as well as connections and networks to their role as board members. As argued by Lawler (2009) and Main, Jackson, Pymm, and Wright (2008), boards with directors bringing greater experience in strategic human resource management may be better positioned to assist in the acquisition of information with respect to the human resource activities of senior management. This, in turn, may impact the asymmetry of information between boards and the CEO and allow the board to better monitor strategic human resource management. Practically, this could manifest as boards of directors and remuneration/compensation committees with memberships that are more skilled and better informed about both the measurement and monitoring of human resource strategy (e.g. the development of senior leaders) and with better information about the specific activities of management. Lawler (2009) makes just such a call, noting that less than 20% of boards include members with significant human capital experience. As he most tellingly writes:

> it would be more encouraging if … board members had expertise in management and boards evaluated the human capital management performance of the CEO as regularly and as rigorously as they evaluate the financial management performance of the CEO. (Lawler, 2009, p. 2)

It is worth noting that this relates to expertise about just one of the relevant stakeholders and the associated value brought to the monitoring and control function. As noted by Kaufman and Englander (2005), relevant stakeholders may bring expertise and insight that serve to strengthen the monitoring and control functions of the board over management.

Applying agency and stakeholder theories to the service role of boards of directors

As previously discussed, agency theory has been espoused as a fundamental explanation for the existence of boards of directors and their monitoring/control role (Eisenhardt, 1989; Hillman & Dalziel, 2003). Conversely, it is intuitive that stakeholder theory aligns well with the service and strategy role of the board. If the underlying logic of the firm is as a nexus of contracts with a multitude of stakeholders, then the board of directors provides a more reliable mechanism to understand and address these relationships (Kaufman & Englander, 2005). However, while this has been the overwhelming focus, it is still possible to consider the application of agency theory in relation to the service role of the board of directors. Where agency theory notes that information asymmetries lead boards to spend extensive effort on monitoring and controls, boards of directors that have more effectively and efficiently dealt with these problems will be better able to turn their focus to the service and strategy role. In practice, this might suggest that boards of directors which have identified effective and efficient mechanisms, to either align managerial incentives or to increase the quality of monitoring, will therefore spend more time on the service role, including discussions of strategic human resource management.

As noted by Hillman et al. (2009), the predominance of stakeholder and resource dependence theory in research on boards of directors is driven precisely because it seeks to explain mechanisms for boards to fulfil the service role. Research with respect to board capital can be focussed on stakeholder matters such as human resource strategy to illuminate the impact of directors' outside experiences and relationships in human resource strategy on the firm. Again, Lawler's (2009) admonishment is for boards to ensure that similar efforts are made to recruit professors of human resource management and organisational behaviour as are made to include finance and accounting professors. Stakeholder theories of governance suggest the use of the board of directors to optimise cooperative exploitation of resources between the firm and stakeholders in shared interest (Crilly & Sloan, 2012; Henisz, Dorobantu, & Nartey, 2014; Kaufman & Englander, 2005; Maharaj, 2008). Directors with a strong

knowledge of stakeholder interests (e.g. suppliers, competitors, the industry, etc.) may be able to provide advice and counsel about the environment, needs and approaches of partners and competitors alike that would otherwise be unavailable to the firm, thereby enabling 'best fit.' Directors with particular expertise in strategic stakeholder issues may be able to provide information, advice and service about best practice that might otherwise be unavailable to the firm. In both cases, the social capital of directors (outside connections) may contribute further valuable resources. As such, the theoretically attractive proposition that boards composed of diverse members will be best equipped in strategy and service is compelling.

Conclusion

Agency and stakeholder theories of the firm have played key roles in the discourse of the firm over the past four decades. They have frequently been positioned as diametrically opposed perspectives; one anchored in economic logic and the other having a decidedly moral basis. As such, the tendency has been to treat these views as distinct and without any possibility for unification. However, both are about governance of the firm and each has a role to play for the researcher and practitioner interested in a key body in governance, the board of directors.

We have noted how agency theory lends itself more to the understanding and application of the control/monitoring role of the board of directors. Boards can serve the roles on behalf of owners, and on behalf of other stakeholders, to ensure that interests and actions of managers are aligned with theirs. Similarly, stakeholder theory aligns well with the service role of the board (encompassing both resources and strategy). The involvement of boards in organisational strategy suggests that managers can benefit from assistance in understanding the complexity and diversity of stakeholder interests. We have also argued that, to a lesser extent, agency theory enhances our understanding of the board's service role, and stakeholder theory enhances our understanding of the board's control/monitoring role. Ultimately, the fact that boards of directors serve both control/monitoring and service roles suggests that organisational governance is structured so as to optimise either view of the firm, be it agency or stakeholder.

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