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Toward a Behavioral Theory of Boards and Corporate Governance

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ABSTRACT

Manuscript Type: Review
Research Question/Issue: A coherent alternative to an economic approach of corporate governance is missing. In this paper we take steps towards developing a behavioral theory of boards and corporate governance.
Research Findings/Results: Building upon concepts such as political bargaining, routinization of decision making, satisficing, and problemistic search, a behavioral theory of boards and corporate governance will focus more on (1) interactions and processes inside and outside the boardroom; (2) the fact that decision making is made by coalitions of actors and objectives are results of political bargaining; and (3) the notion that not only conflicting, but also cooperating, interests are parts of the boards' decision making and control over firm resources.
Theoretical Implications: The consequences are a new research agenda for boards and corporate governance. The agenda will focus on actual instead of stylized descriptions of board behavior. In a behavioral perspective the emphasis on problems of coordination, exploration, and knowledge creation may dominate over problems of conflict of interest, exploitation, and the distribution of value. A future research agenda based on a behavioral framework calls for novel and adventurous research designs.
Practical Implications: A behavioral theory of boards and corporate governance will be closer to actual board behavior than the traditional economic approach and research about boards and corporate governance may thus become more actionable for practitioners.

Keywords: Corporate Governance, Board Processes, Board Composition, Board Leadership, Board of Director Issues

INTRODUCTION

Corporate governance research addresses the nature of interactions and relationships between the firm and its stakeholders in the process of decision making and control over firm resources. In the corporate governance literature there has been a considerable interest in boards of directors. The majority of board research has been dominated by the well-known agency theory perspective (Jensen and Meckling, 1976; Fama and Jensen, 1983). Research in this tradition typically emphasizes formal incentives and control mechanisms, with a focus on how boards of directors may protect shareholder interests from opportunistic and self-serving managers through bonding or monitoring activities, particularly in situations where contracts are incomplete. However, despite its popularity in the field of corporate governance, the extensive body of related empirical research has so far yielded conflicting and ambiguous results.

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The general unease about the conflicting and ambiguous results has led to calls for new directions and alternative theorizing in research on boards and corporate governance (Daily, Dalton and Cannella, 2003; Gabrielsson and Huse, 2004; Davis, 2005; Hambrick, Werder and Zajac, 2008). In line with these calls, a growing number of studies have emphasized the need to more closely study behavioral processes and dynamics in and around the boardroom to better understand conditions for effective corporate governance (e.g., Huse, 1998; Zajac and Westphal, 1998; Forbes and Milliken, 1999; McNulty and Pettigrew, 1999; Westphal 1999; Westphal, Seidel and Stewart, 2001; Huse, 2005; Leblanc and Schwartz, 2007). However, "behavioral" studies of boards and corporate governance are scattered across disciplines and research traditions, and they apply different methodologies and assumptions (Huse, 2005). As such, understanding boards and corporate governance in a behavioral framework does not yet provide a coherent alternative to the agency theory perspective in corporate governance. Therefore, the objective of this paper is to take some steps toward the development of a behavioral theory of boards and corporate governance.

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In this review paper, we will summarize and integrate previously published research with the aim of developing a behavioral framework for a future research agenda on boards and corporate governance. Based on the review, we contend that building upon *A Behavioral Theory of the Firm* (Cyert and March, 1963), a behavioral theory on boards and corporate governance, may provide the foundation for an emerging avenue of research. We argue that boards, in reality, may be less concerned with solving conflicts of interests and rather more concerned with solving problems of coordination and managing the complexity and uncertainty associated with strategic decision making (McNulty and Pettigrew, 1999; Rindova, 1999; Roberts, McNulty and Stiles, 2005). The main feature characterizing the behavior of boards in a behavioral framework is in this respect the limited ability of organizational actors to effectively gather and process information (Cyert and March, 1963; Argote and Greve, 2007). This will, in turn, necessitate the collection and coordination of dispersed knowledge through planning and control procedures. Corporate governance institutions, such as boards, can then be primarily conceived of as problem-solving institutions that reduce complexity, create accountability, and facilitate cooperation and coordination between stakeholders. Such a framework consequently challenges the dominant agency perspective, which deals with boards primarily as a deterrent to managerial self-interest in the context of formal contracts and (primarily) extrinsic rewards.

The paper contributes to research and the literature on boards and corporate governance in several ways. First, it is more connected to empirical observation than is much of the present research about boards. So far, research on boards and corporate governance has heavily relied on unquestioned behavioral assumptions (Pettigrew, 1992; Pye and Pettigrew, 2005) and a majority of empirical studies treats behavioral interactions and decision-making processes largely as intervening unmeasured constructs (Forbes and Milliken, 1999; Gabrielsson and Huse, 2004).

Secondly, and in line with the behavioral theory of the firm (Cyert and March, 1963; Argote and Greve, 2007), we regard the firm as a nexus of coalitions of stakeholders, each with different objectives. Consistent with this conception of the firm, the role of the board is conceptualized here as one of mediating between various coalitions of internal and external actors and establishing controls to ensure that organizational effort is directed toward achieving the goals that the dominant coalition has set.

This complements our third contribution, which is the premise that the purpose of the board is to enable cooperation. However, this takes place not only by solving conflicts among coalitions of stakeholders and exerting control, but also, and perhaps even more importantly, by solving problems of cooperation and coordination and engaging in collective processes of organized information and knowledge gathering. As such, a board's contribution to firm performance is expected to derive mainly from its involvement in enabling cooperation, as well as collecting and using relevant and timely knowledge, rather than from the reduction of agency costs. Consequently, this paper calls for the application of the key concepts and mechanisms of *A Behavioral Theory of the Firm* to corporate governance research. These are bounded rationality, satisficing behavior, the routinization of heuristic decision-making practices, and political bargaining (within the context of the corporation as a coalition of stakeholders). These concepts have been largely overlooked in the contemporary research on boards and corporate governance.

The rest of this paper is organized in four sections. In Section Two we discuss the behavioral theory approach within the broader context of the research streams that deal with boards and corporate governance. Section Three summarizes the main theoretical concepts from the behavioral theory of the firm that have been applied in recent board research. They provide the basis for a behavioral theory of boards and corporate governance. Thereafter, in Section Four we discuss the different items on an emerging research agenda of a behavioral theory of boards and corporate governance. Section Five concludes the paper with a summary of the major implications of a behavioral framework.

MAJOR AVENUES OF RESEARCH IN THE STUDY OF BOARDS AND CORPORATE GOVERNANCE

Before outlining some fundamentals of a behavioral theory of boards and corporate governance, we will first attempt to position the behavioral approach within the context of the major research streams in contemporary studies of boards and corporate governance. To structure our discussion in this section, we have identified six major research streams that each has addressed corporate governance in terms of corporate structure, interactions, and decision processes (Van Ees and Postma, 2004). These are presented in Table 1. The first two research streams deal with the issue of formal structure; that is, with organizational design. The second two deal with behavioral interactions, which refer to the interplay between actors who work closely together inside and outside the boardroom. The final two research streams have dealt with decision processes, which refer to the making and shaping of strategic decisions, their implications, and the processes through which these decisions evolve.

Each pair of research streams can in turn be further differentiated by their focus either on internal or external relationships (see also Hambrick *et al.*, 2008). Internal relationships are relationships in and around the board, between board members and groups or coalitions of internal actors or stakeholders. External relationships refer to relationships between board members and groups or coalitions of external actors or stakeholders. The practice of distinguishing between external and internal actors in research on corporate governance is far from new and has its background in the potential conflict of interest between different actors in and around the organization. A common way to identify internal and external actors is to make a distinction based on whether they operate within the strategic apex of the company (i.e., those who have the authority to make decisions and take actions within the firm) or if they are placed outside this apex (i.e., those who seek to influence and control decisions and actions) (i.e., Mintzberg, 1983). In the corporate governance literature, shareholders are often considered to be the most important external actors (Monks and Minow, 2008). However, the list of external stakeholders

TABLE 1
Research Streams on Boards and Corporate Governance

	Internal relationships	External relationships
Structure	I. Command and control – *Incentives and goal alignment* – *Monitoring and bonding*	II. Codification and compliance – *Law, codes, contracts and regulation*
Interactions	III. Collaboration and conflict – *Political bargaining* – *Power and trust* – *Conflicts and emotions*	IV. Coordination and cooptation – *Social networks and director interlocks* – *Social elites and social movements*
Decisions	V. Cognition and competence – *Decision–making biases* – *Cohesiveness and commitment* – *Diversity and competence*	VI. Conformity and ceremony – *Institutional embeddedness and identity* – *Norms, symbolism, language and rhetoric*

may also include customers, suppliers, competitors, tax collectors, and other government agents (Freeman and Reed, 1983; Huse and Rindova, 2001). The CEO and the top management team are often considered to be the most important internal actors. Controlling shareholders are, in many cases, also considered to be internal actors.

As the objectives of this article are to develop a theoretical framework and a future research agenda grounded in behavioral theory, our review is neither fully comprehensive nor does it present a detailed account of all relevant studies within the vast area of research on boards and corporate governance (for more detailed reviews and discussions see, e.g., Daily *et al.*, 2003; Gabrielsson and Huse, 2004; Huse, 2005). Rather, we aim instead to illustrate the different themes and topics that have garnered interest among scholars working in the field.

Formal Structure

Command and Control. Corporate governance research is dominated by economic theories that assume that a firm functions in line with its formal structure (Daily *et al.*, 2003). As a result, the dominant research stream in studies of boards and corporate governance has been concerned with the study of command and control problems among internal stakeholders within the firm. This is the classical domain of agency theory (Jensen and Meckling, 1976; Eisenhardt, 1989), which has as its focus the contract between principals (the owners of the firm) and agents (the top management). According to the agency model, both principals and agents are assumed to behave rationally and opportunistically. In addition, both sets of actors are assumed to have conflicting goals (to varying degrees) and to suffer from information asymmetries. From these assumptions, agency theory posits that the relationship between principals and agents may be subject to inefficiencies, to the extent that asymmetric information prevents effective monitoring of the agents' actions by the principals. The solutions to these problems in an agency theory-based framework have been the development of formal incentive and control mechanisms and the assignment of a formal monitoring role to the board of directors (Fama and Jensen, 1983). As a result, research within this stream has focused on finding optimal incentive and monitoring structures by exploring the effects of various board structures, such as CEO duality, board composition, and board (member) independence, on firm performance (Rhoades, Rechner and Sundaramurthy, 2001; Ellstrand, Tihyani and Johnson, 2002; Randøy and Nielsen, 2002).

Codification and Compliance. A related stream of research has addressed the formal structure of the corporation vis-à-vis its external stakeholders. Here too, the corporation is regarded as a nexus of contracts and, similarly, the predominant theories in this field include agency theory (Jensen and Meckling, 1976), as well as transactions costs economics (Williamson, 1984, 1988) and several other contracts-based theories. Again, actors are assumed to behave rationally with the objective of maximizing their own benefits under conditions of incomplete or asymmetric information. The design of corporate governance regulation is considered as part of this research stream. These regulations include corporate governance legislation and general codes of corporate governance that structure and codify the relationships between the corporation and its external stakeholders (Kirkbride and Letza, 2004; Monks and Minow, 2008).

Interactions and Relationships

Collaboration and Conflict. Whereas the first two research streams are dominated by the law and economics discipline, studies of behavioral dynamics in and around the boardroom have primarily been examined from disciplines such as sociology and social psychology. However, there is a stream of corporate governance research that deals explicitly with board behavior and has addressed interactions and relationships between board members and other internal actors. Here, the focus has primarily been on conditions that contribute either to collaboration or conflict in CEO-board relationships. This literature draws on a wide array of theoretical perspectives. Stewardship theory has been one of the more prominent perspectives in successfully challenging the agency theory perspective (Donaldson and Davis, 1991; Davis, Schoorman and Donaldson, 1997). It is noteworthy that, although the behavioral assumptions underlying stewardship theory contrast sharply with those of agency theory, it has more recently been considered as a complementary, rather than competing, perspective in shaping our understanding of the conditions that influence effective board governance (e.g., Shen, 2003; Sundaramurthy and Lewis, 2003). Popular themes in this research stream have been how CEO characteristics (tenure and experience), social ties, demographic similarity, and timing of directors' appointment affect power and politics in the upper echelon of the organization (Finkelstein and D'Aveni, 1994; Westphal and Zajac, 1995; Zajac and Westphal, 1996a; Westphal, 1999; Westphal and Bednar, 2005; Westphal and Stern, 2006).

Coordination and Cooptation. The fourth research stream has focused more on issues of coordination and cooptation through directors' interorganizational networks. These issues have primarily been analyzed in the context of resource dependency theory, which explains how organizations seek to connect to their environment in order to secure a stable flow of resources (Pfeffer, 1972; 1973; Pfeffer and Salancik, 1978; Provan 1980). From the resource dependency perspective, boards can link the organization with its environment by establishing important contacts and providing access to timely information through personal and professional networks (Boyd, 1990; Hillman, Cannella and Paetzold, 2000; van Ees and Postma, 2004). One way of linking the organization with its environment is by means of co-opting representatives from important constituencies in the environment. Such co-optation practices can be seen as instrumental acts that aim to achieve organizational goals by reducing uncertainty, acquiring resources, or diffusing information (Pfeffer and Salancik, 1978).

The extensive research on director interlocks is a related stream of studies that provides further insight into the power dynamics associated with multiple board memberships (Richardson, 1987; Davis, 1991; Haunschild, 1993; Mizruchi, 1996; Zajac and Westphal, 1996b; Haunschild and Beckman, 1998; Gulati and Westphal, 1999; McDonald, Khanna and Westphal, 2008). In particular, these studies have focused on the ways in which director interlocks influence the diffusion of technology, policy and strategy, as well as provide a social context that favors continued managerial dominance. This research stream has examined how power, trust, and resources flow between organizations and foster cooperation so as to increase organizational effectiveness.

Decisions

Cognition and Competence. While the two previous research streams are focused on interactions and relationships between board members and other actors, the two remaining streams of research both deal with strategic decision making. Specifically, they address the making and shaping of strategic decisions, as well as the context and processes through which these decisions evolve among internal and external actors. In this vein, the fifth stream concerns studies that deal with the decision-making context in and around the boardroom. The starting point for many of these studies is the observation that the contradictory findings in mainstream governance research can be attributed to the complexities of board decision making. Many scholars have therefore argued that there is no other way to analyze this proposition than to focus on actual decision-making behavior and the underlying behavioral processes of boards (Huse, 1998; Pye and Pettigrew, 2005). Although research on these issues can be characterized as highly eclectic, some studies have employed theories and concepts from the fields of cognition and small group decision making (Forbes and Milliken, 1999; Rindova, 1999; Gabrielsson and Winlund, 2000; Huse, Minichilli and Schøning, 2005; van Ees, van der Laan and Postma, 2008). Another feature of research in this stream is the influence of director competency, experience, and knowledge on effective board functioning and the making and shaping of strategic decisions (Westphal and Fredrickson, 2001; Zahra and Filatotchev, 2004; Kula and Tatogly, 2006).

Conformity and Ceremony. Finally, we identify a sixth research stream that is mainly concerned with how processes of conformity and ceremony vis-à-vis external actors influence decisions and outcomes. The main perspective in this stream has been institutional theory, which is a theoretical perspective that addresses how interdependencies between corporate and other societal institutions make organizations conform to the accepted norms of their populations (DiMaggio and Powell, 1983). Board appointments and social network ties are in this perspective seen as enabling board members to learn about existing norms of appropriate beliefs and behaviors in the relevant industry or country (e.g., Westphal *et al.*, 2001; Jonnergård, Kärreman and Svensson, 2004; Aguilera and Cuervo-Cazurra, 2004). Board members persuade each other that certain corporate governance structures and policies are efficient even if evidence is lacking. Boards may, in this respect, be subject to processes of social construction, whereby the adoption of practices fulfills symbolic rather than, or in addition to, efficiency requirements (Westphal *et al.*, 2001). Consequently, director interlocks and multiple board memberships can, from this perspective, be expected to encourage imitation; not only through conscious choice, but also as it triggers the adoption of taken-for-granted board behavior through less explicit socialization processes (Carpenter and Westphal, 2001).

An alternative perspective in this stream of research focuses on the field of rhetoric and impression management (e.g., Zajac and Westphal, 1994; Westphal and Zajac, 1998; Pye, 2002; 2004). This perspective studies the practice of symbolic management as an instrument to connect the decisions and behavior of the organization to the expectations, rules, and norms in the business-environment. Thus, the organization may assimilate the special order and formal behavior demanded by custom.

Studying Board Behavior: A Call for a Coherent Behavioral Framework

In our view, research streams three through six incorporate the behavioral approach and thus represent an alternative to the dominant economic theorizing on boards and corporate governance. As such, our review illustrates the argument that behavioral studies of corporate governance are scattered across disciplines and research traditions, applying different methodologies and behavioral assumptions. This observation is in line with the growing consensus among scholars of boards and corporate governance that there is a need for theoretical pluralism. In fact, the idea that the different theories provide complementary perspectives, and that none of them can independently provide a full explanation, seems to have gained some ground in the field (e.g., Hung, 1998; Hillman and Dalziel, 2003; Lynall, Golden and Hillman, 2003).

We recognize the value of theoretical pluralism at this stage of corporate governance research. However, we would also like to propose that the behavioral perspective is in need of some commonly accepted core concepts. Surprisingly few studies, in which behavioral research on boards has been conducted, have challenged the dominant agency paradigm. Instead, these studies often argue for the need to include behavioral interactions and processes as intervening variables between boards' structural features and firm outcomes (Gabrielsson and Huse, 2004). As such, current behavioral research on boards and corporate governance does not provide a true alternative to the economics research tradition. In our view, the ability to provide such an alternative requires that we first develop a distinct set of commonly-accepted behavioral concepts. Only then can we embark on future research efforts with clarity and consistency.

To be sure, we must point out that some studies have applied various aspects of the behavioral approach in their research. These studies present alternatives to the economics paradigm to the extent that they incorporate assumptions that more accurately capture the processes and behavioral dynamics in and around the boardroom (e.g., Pettigrew, 1992; Huse, 1998). One concept that has been applied is bounded rationality together with the related issue of satisficing behavior among decision agents (Osterloh, Frey and Frost, 2001; Hendry, 2002; 2005). Another concept that has been applied is the routinization of heuristic decision-making processes (Ocasio, 1999; Rindova, 1999; Carpenter and Westphal 2001; Zahra and Filatotchev, 2004). Finally, some studies have applied the concept of political bargaining within the context of corporations as coalitions of stakeholders (Pearce, 1995; Huse and Rindova, 2001). This research challenges the assumption that shareholders are the a priori defined principals and that corporate goals (i.e., maximizing shareholder value) are unique, given, and stable over time. Interestingly, all these issues and concepts can be traced back to what was introduced almost 45 years ago as *A Behavioral Theory of the Firm*. In the next section we will further discuss and develop them as core concepts that may potentially serve as a foundation for a behavioral theory of boards and corporate governance.

BEHAVIORAL THEORY CONCEPTS IN BOARD RESEARCH

A Behavioral Theory of the Firm has, since the pioneering studies of Simon (1945; 1955), March and Simon (1958), and Cyert and March (1963), been acknowledged as a main perspective for understanding organizational behavior and decision-making (see also Argote and Greve, 2007). Yet little of this rich body of knowledge has spilled over to mainstream studies of boards and corporate governance. However, we believe that this intellectual tradition may serve as a fruitful conceptual foundation for future behavioral studies of boards and corporate governance. The *Behavioral Theory of the Firm* is built around the well-known key concepts of bounded rationality, satisficing, and problemistic search, the routinization of decision making in standard operating procedures, and the dominant coalition (Argote and Greve, 2007). We will shortly introduce these concepts before discussing their implications for theory development in the field of boards and corporate governance.

Bounded Rationality

The concept of bounded rationality has, to some extent, been addressed in recent studies of boards and corporate governance (Ocasio, 1999; Osterloh *et al.*, 2001; Hendry, 2005). The concept refers to the notion that decision makers in organizations experience limits in their ability to process information and solve complex problems (Simon, 1955, March and Simon, 1958; Cyert and March, 1963). Studies have shown that rationality is costly, and applying rational rules in addressing issues and problems with great complexity leads to great cognitive effort (Greve, 2003: 13). The conclusion made from these studies is that upper echelon decision making calls for simplifying decision rules, as the complexity of the business environment makes it impossible to completely understand all linkages among variables around them. Bounded rationality does not necessarily imply that actors do not attempt to maximize utility – only that they are unable to do so due to constraints on their decision-making capabilities. In this respect a behavioral approach may expand the scope of research to include such factors as cognitive biases and incompetence as explanations for inefficient and ineffective decision making (Foss, 2001; Hendry, 2002).

The cognitive bias of organizational actors only allows for an imperfect mapping of the decision-making environment and rather limited, imprecise, and selective information processing. From this perspective, the limited competence and awareness among an organization's members may represent a much more likely cause of organizational inefficiencies and failure than straightforward opportunism, which more or less assumes that individuals have a full understanding of the opportunities available to them (Hendry, 2002). In the literature this notion of bounded rationality has been called "truly bounded rationality" (Osterloh *et al.*, 2001; see also Radner, 1996).

Satisficing Behavior and Problemistic Search

A second key concept that has been addressed in recent research originating from *A Behavioral Theory of the Firm* is satisficing as a behavior of decision makers (Hendry, 2002; 2005). Satisficing behavior implies that actors tend to accept choices or judgments that are "good enough" based on their most important current needs rather than searching for optimal solutions. For corporate governance, the introduction of satisficing behavior, as opposed to optimizing behavior, potentially reduces the gains from behaving opportunistically. As such, this may reduce the relevance of opportunistic behavior as one of the most important drivers of corporate governance research and open up the field for alternative perspectives. Decisions can, in this respect, not be regarded as optimal solutions to problems – they can merely reflect solutions that satisfy particular aspiration levels (Cyert and March, 1963; see also Levinthal and March, 1993). These aspiration levels are in turn determined both by history and the social environment. The historical aspiration level is a function of the organization's past performance. The social aspiration level is set by reference to meaningful reference groups.

The notion of satisficing behavior rests on the observation that decision-makers are primarily concerned with immediate problems and short-run solutions, something that has generally been referred to as "problemistic search" (March and Simon, 1958; Cyert and March, 1963). Problems are, however, only recognized to the extent that an organization has failed to satisfy one or more of its self-imposed goals, or when such failure can be expected in the near future (Cyert and March, 1963). Problem recognition itself is primarily driven by attention allocation and selection biases. When faced with a problem, decision makers can therefore be expected to search for solutions using simple heuristics or decision-making routines. The problem is regarded as solved as soon as an alternative is found that satisfies current goals, or where goals have been revised to a level that makes available solutions acceptable. Decision making in the behavioral theory is consequently seen as an experiential learning process, in which a firm adapts incrementally to its changing environment through learning and experimentation. Thus, decision makers learn by trial and error what can be done, and they adapt their goals, attention rules, and search rules accordingly.

Routinization of Decision Making

A third key concept that recent research has brought to the fore is that boards of directors operate from the basis of "routines" that are built up over time (Ocasio, 1999; Zahra and Filatotchev, 2004). Routines have also been referred to in the literature as performance programs (March and Simon, 1958) or standard operating procedures (Cyert and March, 1963). Here, routines can be understood as the codified memory of the organization; embodying the past experience, knowledge, beliefs, values, and capabilities of the organization and its decision makers (March and Simon, 1958; Cyert and March, 1963). Routines consist largely of experiential knowledge, which may be tacit and hard to codify. Routines can be seen as successful solutions to problems that store and reproduce experientially acquired competencies, which can then be repeated over time.

The implication is that routinization of decision making is an important source of control and stability, which both enable and constrain organizational action. On the one hand, routines conserve the cognitive abilities of board members, and serve to channel and limit conflict among them. On the other hand, they direct attention to selected aspects of identified problem situations (Cyert and March, 1963). Rules and routines are hence not purely passive elements; rather, they serve as socially and historically constructed programs of action that direct attention to selected aspects of a problem situation. As such, they also create decision-making biases. Decision makers, however, are not victims of history; routines can be changed by learning processes, such as through imitation, or through trial and error. Thus, both routinization and unlearning play a central roles in a behavioral theory framework.

Political Bargaining in the Context of Corporations as Coalitions of Stakeholders

A fourth key concept from *A Behavioral Theory of the Firm* that has been addressed in recent research on boards and corporate governance is political bargaining in the context of the firm as a coalition of stakeholders or actors (Pearce, 1995; Huse and Rindova, 2001). Through this perspective, organizations can be depicted as complex political systems with agents organized in coalitions, and some of them further organized into sub-coalitions (March, 1962; Cyert and March, 1963). Coalition partners may have distinct preferences and objectives, which make negotiation and bargaining among coalition members common practice. Shifting coalitions of organizational actors affect organizational decisions, goal setting, and problem solving processes. Goal conflicts are solved through political bargaining rather than through objective alignment by economic incentives. Disagreement about organizational goals is dealt with in the context of ongoing bargaining processes among coalitions that pursue alternative objectives and priorities. Different coalitions may pursue conflicting goals, and organizations may encompass a variety of possibly conflicting and inconsistent goals by pursuing them sequentially. Goal formation is thus achieved by a series of procedures, including the application of local rationality and acceptable level decision rules, as well as sequential attention to goals (Cyert and March, 1963).

The procedures for resolving conflicts do not necessarily lead to a consistent set of goals in the organization. This means that organizations can most of the time be expected to have a considerable amount of latent conflicts and goals. Contrary to most corporate governance research, goal formation is seen as the outcome rather than the beginning of the bargaining between coalitions. As such, goal formation and goal conflicts may drive the search for additional information and knowledge. In fact, from such a learning perspective, goal congruence and consensus may even be a hindrance rather than a stimulus to organizational development. In view of their formal role as "the strategic apex" of the organization, the board of directors will obviously play an important role in this process of goal formation.

Summary: The Behavioral Approach to Understanding Boards and Corporate Governance

The basic concepts underlying organizational decision-making in *A Behavioral Theory of the Firm* have been highlighted above. In this approach, organizational actors seldom base decision making on an overall calculation that takes into account all of the possible consequences of their decisions. Instead, if a problem area is recognized, it triggers a search for possible solutions that ends when a "satisfactory" solution is found. Moreover, actors rely on routines and heuristics that provide them with readily available solutions and procedures for the enactment of organizational decisions. Finally, conflict resolution and goal formation are seen as the result of an ongoing process of political bargaining among coalition members. In our view, this conceptualization of organizational decision making represents an interesting alternative to the currently dominant approach in corporate governance, which regards organizations as monolithic entities where individuals rationally decide how to reach a unified and a priori defined goal. In the next section, we will elaborate upon the implications of such an approach for a research agenda of a behavioral theory of boards and corporate governance.

A RESEARCH AGENDA FOR A BEHAVIORAL THEORY OF BOARDS AND CORPORATE GOVERNANCE

A behavioral theory framework for understanding boards and corporate governance will first and foremost start from the description of actual board behavior, rather than focusing on stylized concepts and constructions. In many ways the accurate and precise description of what boards actually do provides the starting point for theory building. However, the aim is to develop theory that transcends the specific context that is described. Therefore, building upon the four core concepts developed in the previous section, the following research agenda of a behavioral theory of boards is proposed.

Bounded Rationality

First, the emphasis on bounded rationality in a behavioral theory of boards and corporate governance will imply that board members cope with uncertainty by complexity-reduction and by routinely simplifying and structuring information through their perceptual filters and pre-existent knowledge structures (Rindova, 1999). By applying simple decision-making heuristics, directors may in this respect enact decision-making scripts (internalized, for instance, from their experience in other boards) to solve strategy and monitoring problems in the current organization or board. Indeed, mimicry can be an important problem-solving device (di Maggio and Powell, 1983). It is also consistent with the idea that the more deeply particular decision routines are encoded in the organizational memory, the more likely they are to be recalled and enacted later in problem situations that are perceived as similar. The reliance on established rules in board decision making facilitates action by presenting board members with readily available solutions for organizational problems (Ocasio, 1999) and may also increase the board's ability to legitimate and defend its actions and decisions (Westphal and Zajac, 1998). However, such decision making by no means guarantees the best possible decisions and may also lead to myopia and inertia. For corporate governance research, the above implies that the previous experiences of board members, their expectations and reference groups, as well as their routine procedures for information processing and learning, are highly relevant for our understanding of board decision making and the limits on the information with which board members must cope (Spender, 1989).

To conclude, the first item on the research agenda of a behavioral theory of boards and corporate governance should be a careful analysis of the actual routines and mimetic processes observable in and around boards. This may increase our insight into the ways in which boards and their members routinely use their past experiences in similar settings as scripts for solving problems in the current situation (Ocasio, 1999; Westphal *et al.*, 2001). In addition, an analysis of the norms of board behavior, which can be viewed as another source of memorized socially constructed expectations, may yield additional insights in explaining behavior in and around boards.

Satisficing

Secondly, and moreover, the behavioral approach will emphasize the satisficing nature of board decision-making outcomes (Hendry, 2005). Satisficing as the guiding principle for decision making, instead of trying to capture all opportunities to maximize payoffs may likely reduce opportunism between organizational actors (Baumol, 2004). The search for workable problem-solving heuristics is myopic and will be aimed at finding solutions to immediate problems of accountability. Alignment with sub-goals, rather than an exclusive focus on a profit objective, may furthermore help maintain focus on tasks and duties in the organization and in sustaining intrinsic motivation (Osterloh and Frey, 2004). Moreover, the existence of alternative goals in the behavioral approach may provide important inputs for additional information and knowledge. In fact, the diversity of goals among different coalitions of actors can be considered beneficial, since it stimulates the discovery and active search for new knowledge as a by-product of the goal-conflict resolution process. Diverse board members with experiences from different industries and companies will vary in their domain knowledge, the problems they have been exposed to and the problem solving skills they have developed (Rindova, 1999). New knowledge can, in this respect, enter into the board decision-making process through the adjustment of aspiration levels and the formation of alternative dominant coalitions. These conditions will in turn bring greater variety to the problems that the board identifies and the solutions it develops.

Thus, the second item on the research agenda of a behavioral theory of boards and corporate governance should be a careful analysis of how boards contribute to the process of goal formation within organizations. In addition, examining the position and political role of boards in the context of the goal formation process may extend our knowledge of the role of the board in organizational decision making.

Problem Solving

A third item on the research agenda should be the analysis of actual problem solving inside and outside the boardroom. We expect that this may well offer new insights into the specific behaviors and actions of board members that lead to certain decisions by boards of directors (Forbes and Milliken, 1999). A behavioral theory of boards and corporate governance will in this respect reject the notion that boards make optimal decisions based on a complete evaluation of all possible alternatives. Instead, the limits of bounded rationality prohibit the availability and understanding of a complete array of alternatives, which means that simple heuristics will be used to process the gathered information. Satisficing board members can thus be expected to deal with organizational problems by applying norms, myopic problem-solving heuristics, and memorized routines to reduce the complexity of decision making. In particular, the decisions in the current period are informed and shaped by the environmental feedback that board members receive from their earlier decisions (Cyert and March, 1963). Learning processes among board members can in this respect be expected to be "operationalized" in the form of procedures and rules for problem solving, information gathering, and decision making. These procedures and rules can furthermore develop and become institutionalized over time through the regular execution of board work (Ocasio, 1999; Zahra and Filatotchev, 2004) but they may also be modified or unlearned when situations or circumstances in the organization is changed (Akgün, Byrne, Lynn and Keskin, 2007).

In sum, relevant research questions on the research agenda of a behavioral theory of boards and corporate governance will be how and why boards rely on general rules and routines developed from past experience (heuristics) to solve problems and make decisions. In addition, addressing the questions of how, why, and under what conditions boards reinforce, change, or unlearn general rules and routines used to solve problems and make decisions can also be considered as relevant.

Objective Setting

Fourth, current theorizing on corporate governance takes corporate objectives by and large as given. By contrast, in a behavioral perspective on goal formation and conflict resolution, it is first observed that the governance of the firm will be based on the conception of the corporation as a nexus of coalitions of actors. Corporate actors may have conflicting interests and will achieve their goals through changing coalitions in the bargaining process within the corporation. The behavioral perspective on boards and corporate governance would hence primarily place particular emphasis on the analysis of the role and position of the board in the process of organizational decision making rather than on the outcomes (performance) or the decision as such.

In explaining the role and position of the board in the process of organizational decision making, a behavioral theory of boards and corporate governance will focus on the political aspects of board behavior. A behavioral theory of boards and corporate governance may in this setting analyze boards' involvement in the political bargaining in order to achieve cooperation between coalitions of actors or to establish the so-called dominant coalition (Ocasio, 1999; Hendry, 2002). Following upon the analysis of power and trust relationships, the analysis can be extended to the more managerial aspects of political behavior. This includes how the symbolic, rather than substantive, aspects of stakeholder behavior and expectations may be managed to benefit the interests of the dominant coalition of actors (Huse and Eide, 1996).

In political bargaining, the position of the board cannot be regarded as unproblematic. Indeed, the formal role of the board is to consider "the best interest of the firm" only. However, in a political context, the question as to what the best interest of the firm is cannot be answered without reference to context and the existing coalitions of stakeholders (Huse and Rindova, 2001). In other words, the best interest of the firm is to be defined over and over again in a political bargain process among stakeholder coalitions. Contrary to the current corporate governance research, the behavioral perspective thus emphasizes that the objectives of firms cannot be regarded as the objective fundamentals for board decision making. It also implies that the effectiveness of board decision making cannot be analyzed without taking the board decision-making context into account (Huse, 2005). Perhaps due to the exclusive focus on the relationship with top management, the role of boards in organizational decision making has not been addressed extensively in theories of boards and corporate governance.

In this respect, the role of the board in the political bargaining between the different coalitions can be denoted as an additional next item on the research agenda. Organizations have multiple goals and further research should explore the question of how boards, in practice, deal with that multiplicity. In addition, which board procedures or routines structure the sequence and order of seemingly conflicting goals? Furthermore, is the board's role to intermediate or to arbitrate between the different coalitions in the organization? Or, does the board merely represent the dominant coalition by itself?

Research Design

A future research agenda based on a behavioral framework calls for novel and perhaps venturesome research designs in the study of boards and corporate governance. Empirical research into boards and corporate governance has long been dominated by the use of archival data, whereby the behavior of boards has been inferred from their demographic characteristics (Pettigrew, 1992; Huse, 1998; Gabrielsson and Huse, 2004). In contrast, the research agenda based on a behavioral framework developed in this paper suggests that there is a need to more closely examine actual board behavior and decision-making processes in real business settings. This lends itself towards the use of first-hand empirical data collection methods, such as questionnaire surveys, interviews, and participant observations. Ideally, such efforts will collect longitudinal data from multiple respondents that capture the changing configurations of governance as they evolve over time and that take into account variations in beliefs and perceptions among different corporate actors in the analysis.

There are considerable challenges in gaining access to behavioral processes in and around the boardroom. Some of these challenges are addressed by Huse (2009). In this paper he presents examples of sophisticated survey designs, interviews, case reconstructions, and various approaches to direct observations. Gaining access to observe behavioral processes is deeply rooted in trust. Huse (2009) concludes that individual and stand-alone studies may suffer from various flaws that can be overcome by collaboration among researchers, building on each others' work and ultimately, by the accumulation of knowledge. This is not only related to getting access, but also for the initiation, validation, and publication of research using venturesome methods.

We acknowledge that there will be constraints acting against empirical research in a behavioral approach to boards and corporate governance. For example, fieldwork will be time consuming and labor intensive. There may also be institutional constraints. By this we mean that board research conducted in a behavioral theory has traditionally received little attention and understanding among scholars who are used to work within the mainstream economics approach to corporate governance. However, we believe researchers and doctoral students interested in conducting research in a behavioral approach can overcome such constrains by, for example, engaging in collaborative research efforts. Evidence exists about how collaboration in larger research teams may overcome many of the problems doctoral students will have with respect to the constraints of access and time. For example, more than a dozen students have completed their dissertation based on their involvement in the ongoing health care management project in Minnesota directed by Andrew van de Ven. The development of large research programs related to the topic of boards and corporate governance should thus be encouraged.

CONCLUDING SUMMARY

There have been calls to open up the "black box" of actual board behavior (Daily *et al.*, 2003; Gabrielsson and Huse, 2004). New directions and alternative theorizing in research on boards and corporate governance are needed to meet these calls. Strikingly, the current calls are completely in line with the original aim of Cyert and March 45 years ago in *A Behavioral Theory of the Firm.* Their objective was "to open up the 'black box' of the internal workings of organizations" (Argote and Greve, 2007: 344). Despite the parallel, their ideas and concepts have not been used extensively in the current literature on boards and corporate governance. In this article we have taken some steps in outlining a behavioral theory of boards and corporate governance that, in many ways, challenges the mainstream approach for understanding boards and corporate governance in contemporary research.

First, a behavioral theory of boards and corporate governance will be focused on the interactions and behavioral processes among and between actors in and around the boardroom rather than on the outcomes (i.e., the performance) of boards. Most studies that have explored boards from an economics perspective have more or less neglected actual board behavior. Instead they have analyzed the relationships between ideal-typical board constructs and corporate performance. They have applied unquestioned behavioral assumptions as a basis for prescription where interaction, communication, and information sharing between board members have generally not been assumed to affect the board's work (Pettigrew, 1992; Forbes and Milliken, 1999; Gabrielsson and Huse, 2004). In contrast, for a behavioral theory of boards and corporate governance the actual interactions and behavioral processes in and around boards will be the starting point (Huse, 2005).

However, emphasis on actual board practice is a necessary, but not a sufficient, condition for a behavioral theory of boards and corporate governance. The challenge is to go beyond simple description by developing a limited set of behavioral concepts to explain the decision making of boards as well as the role of boards in organizational decision making. The key concepts in this respect are bounded rationality, satisficing behavior, routinization of heuristic decision-making processes, and political bargaining in the context of the corporation as a coalition of stakeholders. Thus, the core concepts of a new research agenda grounded in the behavioral theory of the firm will address the processes of past-performance evaluation in the context of boards, the search for alternatives, and the decision-making routines and procedures in and around boards.

To start, it can first be argued that a behavioral perspective of boards and corporate governance will focus on decision-making processes rather than structures and outcomes. If structure exists, it is because actors are constructing and reconstructing intentions and accounts and thereby their own and others' identities (Kärreman, Alvesson and Wenglén, 2006). Much more emphasis would also be placed on the effects of past behavior, previous experience, and shared beliefs on the current decision-making behavior in and around boards (Spender, 1989). As such, the emphasis on context and history in the behavioral perspective on boards and corporate governance stands in contrast to a more axiomatic approach taken in economics, where the corporation is a "focus for a complex process in which the conflicting objectives of individuals (some of whom may 'represent' other organizations) are brought into equilibrium within a framework of contractual relations" (Jensen and Meckling, 1976: 311).

Second, a behavioral perspective will conceptualize the corporation as a nexus of coalitions of stakeholders without any a priori assumptions of organizational goals and objectives. Such a starting point may perhaps sound a bit radical, especially compared to the dominant perspective, which states that the principal objective of the corporation is to maximize shareholder value. The behavioral perspective will however emphasize that the setting of goals and objectives are influenced by power plays and politics in and between coalitions. As such, a behavioral perspective will accept that board decision-making behavior is contingent upon the relative power and relationships among various coalitions of internal and external actors. The relative power and relationships between the various coalitions and actors may in turn be contingent upon the different stages of the firm's development (Huse, 1998; Zahra and Filatotchev, 2004), and board composition may reflect the wider power relationships between internal and external actors at the time of board formation (Lynall *et al.*, 2003). The power and influence of the board of directors may change in times of crisis compared to normal times, and various types of crises may change the stakes, power, and activities of various actors (Mace, 1971; Lorsch and McIver, 1989). Consequently, the goals and objectives of the organization may shift as coalitions change. Hence, contingencies related to the firm's industry, as well as the firm's life cycle might affect interactions and relationships among coalitions of stakeholders in and around the corporation in a way that effects both the position and the roles of the board (Lynall *et al.*, 2003; Zahra and Filatotchev, 2004).

Third, a behavioral theory of boards and corporate governance would, in addition to dealing with conflicts resulting from divergent preferences of stakeholder coalitions, emphasize board members' contributions in dealing with the complexity and associated uncertainty related to strategic decisions and the search for existing or new knowledge to solve organizational problems. Because organizational actors have limited cognitive capacity they need planning and control routines to help them analyze complex tasks and to avoid making errors in decision making. The conflicting goals among organizational actors also imply a conflict of cognitive resources, such as, for example, access to attention, knowledge and memory, which in turn influence the perception, or "framing," of the problem situation (Lindenberg, 2003). Participation in the early stages of strategic decision making will, in this respect, enable board members to protect stakeholders' interests through problem identification and problem definition (Rindova, 1999). This suggests that board members contribute to the problem solving process because they offer a variety of experiences and quality of judgment which in turn makes them perform their monitoring tasks more effectively (Andrews, 1980). As such, board members use the strategic problem-solving expertise they have developed in their primary occupations and provide inputs into the cognitive tasks through which strategic decision making is carried out (Forbes and Milliken, 1999; Rindova, 1999). Therefore, in a behavioral perspective the emphasis on problems of coordination, exploration, and knowledge creation may dominate over problems of conflict of interest, exploitation and the distribution of value.

To conclude, we have in this essay summarized and integrated previously published research with the aim to develop a behavioral framework for a future research agenda on boards and corporate governance. Such a framework clearly challenges the dominant agency perspective. However, as we see it, the two perspectives represent markedly different and perhaps equally viable streams in research on boards and corporate governance. At the same time, our research agenda can be considered as an open invitation for additional research and analysis on the topics formulated in our discussion. It is our hope that the arguments underlying these topics may add new perspectives to the existing research agenda on boards and corporate governance.

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