Agency and Institutional Transformation:
The Emergence of a New Corporate Governance Model

By

Stewart James Melanson

A thesis submitted in conformity with the requirements
for the degree of Doctor of Philosophy

Rotman School of Management
University of Toronto

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Rotman School of Management, University of Toronto, 2010

Abstract

This research examines institutional transformation of the board of directors in Canada to a collaborative model in which the board, in addition to its monitoring function, provides a service role by acting as a sounding board to management and providing advice and counsel to management on strategic issues. This thesis also examines how director search, likely initiated by the ‘Enron’ scandals, led to some boards adopting a new model of practice that directors deemed more efficacious and possessing legitimacy, bringing together the old and the new institutionalism in institutional change processes. Legitimacy was drawn from guidance from a professional association for directors that outlined how boards could become strategic asset to the firm that was consistent with a stewardship model of governance that saw boards collaborative with management. It is also argued in this thesis that following the Enron scandal, directors searched for a model of practice that would be more efficacious such that their fears of liability were reduced. In searching for and adopting a new model of practice, the collaborative board, it is also argued that adoption requires coupling to the technical core (enacted), as opposed to symbolic, if it is to be effective. This research studies directors and senior management of public firms of the TSX Composite by way of survey methods. The findings
provide support that the board is evolving in Canada to a new collaborative model and that the model of practice appears to be enacted (coupled) as opposed to symbolic (decoupled). Further, the results did not find that collaborative boards are impaired in their monitoring function and support is found that the board’s monitoring role may actually be enhanced. These results are discussed as well as future research directions and limitations of the study.

Key Words: Corporate Governance, Institutional Theory, Institutional Change, Agency Theory, Stewardship Theory
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Chapter One

Introduction
Corporate governance has been a growing topic of interest with respect to public firms and their performance in the advanced capitalist economies (Daily, Dalton and Canella, 2003). The role of the corporate board of directors in oversight of public firms gives them a central role as the ultimate authority within the corporation with a fiduciary duty to serve the long term interests of the corporation on behalf of the owners (Hansell, 2003). Failure of the board in their oversight duties can have significant harmful economic repercussions (Monks, 2005) which makes their study of practical importance as well as of interest to academics (Eisenhardt, 1989).

The academic literature has studied the topic of corporate governance from a largely legal-economic approach (agency theory) with an emphasis on the examination of governance reform efforts to improve oversight of the firm and thereby improve firm performance by lowering agency costs (Matsumura and Shin, 2005). The ability to enhance oversight of public firms to improve overall economic well-being is an important topic of study, particularly following perceived failings in governance after a series of scandals often referred to as ‘Enron’ (Monks, 2005; Clarke, 2004). Thus, I initiated collaborative research in 2002 with McKinsey & Company and the Anderson Governance Group that focused on the responses of stakeholders in Canada to governance reform efforts in the aftermath of Enron and other high profile scandals.

Governance reform efforts have been largely guided by agency theory (Daily, Dalton and Canella, 2003) as evidenced by rule heavy legislation such as Sarbanes-Oxley (SOX) which prescribed board structural independence of management (Monks, 2005). Given the agency focus of reform efforts, the research question I posed was if directors would behave more independently of management, i.e., have a more neutral and arms-length relationship, in line with
agency concepts on how firms ought to be governed, as opposed to collegial relations. This question is of importance since there is a literature that suggests director responses to reform efforts have been more symbolic than substantive – reforms to increase director independence are adopted by boards but actual board practices remain largely unchanged (Westphal & Zajac, 2001; Westphal & Zajac, 1998; Westphal, 1998; Zajac & Westphal, 1995). However, the scandals jolted the system (Melanson, Bates and Hennessey, 2003; Greenwood & Hinings, 1996) leading to re-invigorated reform efforts that might lead to more substantive changes in director behaviour (Clarke, 2004). Thus in the face of increased pressures on boards post-Enron, and the dominance of agency in guiding governance reform, I expected directors might acquiesce and behave more neutrally and arms-length with management to increase their independence in practice.

The majority of empirical work on boards has been to examine board structural variables such as separation of the CEO and board chair positions (Westphal, 1999), but in order to examine actual director conduct, survey methods are required (Schmidt and Brauer, 2006; Westphal and Zajac, 2001). Thus survey methods were employed to explore director conduct but surprisingly, the results of the survey, administered to directors of firms listed on the TSX composite in 2004 and 2005, revealed a contradiction to the predicted responses of directors to governance reform efforts following the scandals (Anderson, Melanson and Maly, 2007). The expected response was directors conducting themselves with increased arms-length and neutral relations with management as prescribed by agency concepts (Eisenhardt, 1989). Instead, the findings were that directors were shifting their behaviours in the opposite direction whereby they developed a closer working relationship with management, representing a collaborative model of practice more consistent with stewardship theory (Davis, Schoorman and Donaldson, 1997).
These findings led me to formulate a number of key research questions that are the basis of this thesis. First, if directors are embracing a collaborative model of governance, is its prevalence as a new model of practice increasing with time; will it represent a rejection of the orthodoxy of agency based practice and become the new norm of board practice? Also, will adoption of the new model of board acting collaboratively with management be associated with actual director conduct that is consistent with such a model of practice? Further, closer ties with management are argued by agency theorists to compromise the ability of the board to monitor management (Forbes & Milliken, 1999) although there is research that argues collaborative boards are not so compromised and monitoring could even be enhanced (Westphal, 1999). Thus, does such a model of practice compromise or enhance the monitoring function of the board (is the model efficacious) given that directors develop closer ties with management? Such questions as these lend themselves well to examination through an institutional lens and their exploration was commenced through a new round of survey research which forms the foundation of this thesis.

The new round of research was also collaborative, being in partnership with McKinsey & Company and The Anderson Governance Group. However, it was agreed that I would design research questions and my own theoretical approach separately from my collaborators for the purposes of completing my thesis in conformity with the requirements for a doctor of philosophy degree. As such, while the survey instrument was co-developed with McKinsey & Company and The Anderson Governance Group, I designed specific research questions and the theoretical approach while my collaborators designed their own research questions to create a survey instrument that addressed my questions of interest as well as my collaborators questions of interest – the survey was designed with questions I posed to answer research questions salient to
this thesis while other parts of the survey reflected research questions of interest to McKinsey & Company and the Anderson Governance Group and so are not a part of this thesis.

Some examples of questions in the survey (see Appendix B) that are specific to my collaborators are questions 7, 8, 15-18, 22-25. Questions 7, 8 and 15 to 18 were of interest to The Anderson Governance Group as they perform board evaluation and so they are interested in director responses to questions on the effectiveness of board evaluation and the relationship between the board chair and the CEO. McKinsey & Company was interested in director views on executive compensation structure and adequacy (Q. 22-25). Questions specific to my interests are given in Appendix D and Tables 3 through 6. However, as a consequence of differing research interests, the survey had the potential to become too long and burdensome and so where possible, questions were developed that could answer multiple questions of interest, not just mine or theirs. For example, questions on board knowledge of risk factors facing the firm (Q. 9) were designed for my purposes of testing enactment of the collaborative model while McKinsey & Company could identify gaps in director knowledge for purposes of consulting. Further, I solely developed the hypotheses, model tests and interpreted the findings reported here in this thesis. I now turn to my research approach.

While Institutional theory is concerned with why organizational forms and practices are similar, it is also useful in examining change processes contesting orthodox practice (Greenwood & Hinings, 1996; Oliver, 1991). To explore my research questions above, I use an institutional approach to examine how agency theory is being challenged as the sole legitimate model of governance practice. The persistence of agency based prescriptions for governance reform
despite increasing questions about its efficacy in guiding reform efforts (Dalton, Daily, Certo & Roengpitya, 2003; Sundaramurthy & Lewis, 2003; Westphal, 1999) is due to its long standing status as the legitimate academic line of research in governance representing the established orthodoxy (Greenwood, Oliver, Sahlin and Suddaby, 2008). The persistence of sub-optimal models of practice due to their legitimacy through being widespread in practice (orthodoxy) is a major theme in institutional analysis (DiMaggio and Powell, 1983). Given the orthodoxy of agency based reform efforts, their widespread practice and questions of efficacy in enhancing firm outcomes and guiding board behaviours, it is of interest to examine corporate governance change through an institutional lens. And in particular, from the perspective of director responses to institutional pressures (Oliver, 1991) arising from governance reform efforts following scandals that may be considered a triggering event for substantive institutional change whereby orthodox practice is contested (Greenwood & Hinings, 1996).

It is noteworthy that directors, through behavioural changes in board practices, appear to have challenged the prevailing orthodoxy of agency based reform efforts (Anderson, Melanson and Maly, 2007). Challenging a well established orthodoxy is uncommon but can occur when environmental changes reveal weakness in the current institutional arrangements (Townley, 2002; Selznick, 1948). However, institutionalists have also posited the need for legitimacy of new practices that early adopters of a new model can point too as support for their challenging orthodox practice (Sanders and Tuschke, 2007). The collaborative model does have a source directors can point too to legitimate adoption and that is a report by the National Association of Corporate Directors (NACD) released in 2001 that supported a collaborative role for the board of directors. The NACD, as a professional association for directors, is an important source of
guidance to directors on what is acceptable and legitimate practice (Greenwood, Suddaby and Hinings, 2002). Thus, early adopters of a collaborative model of practice could rely on guidance from the NACD to justify adoption. At the same time as the release of the NACD report (NACD, 2001), corporate scandals initiated a new round of regulation focused on governance reform.

The scandals collectively riveted public attention to governance issues and prompted sweeping regulatory change (Sarbanes-Oxley – SOX) on a scale not seen since the great depression era with the passing of the Securities Act of 1934 (Matsumura & Shin, 2005). The purpose of the new regulation, in line with agency concepts was to increase board independence in structure and in practice – behave with neutral relations with management. How directors actually behave has practical implications if director conduct, as noted, is merely symbolic as opposed to enacting practices prescribed by governance reform efforts (Westphal and Zajac, 1998); since this suggests that reform efforts may be adopted symbolically only and remain decoupled from the technical core of board activities (Westphal and Zajac, 2001). That is, boards adopt to maintain legitimacy but despite adoption, practice is not coupled to the technical core such that old behavioural norms remain embedded.

Indeed, the board has often been referred to as largely a symbolic or ceremonial body (Hansell, 2003; Herman, 1981) with little influence on firm performance despite the fact that the board of directors is legally the highest authority in the body corporate (Judge and Zeithaml, 1992). The recent passage of rule-heavy legislation in 2002 (SOX) and a perception of greater exposure of directors to liability after the scandals (Monks, 2005) raised the question of how boards might respond to the newly invigorated reform efforts – behave differently or maintain
the status quo? While ‘Enron’ may have induced legislation pushing boards to adopt practices aimed at increasing board structural independence, as already noted, prior research (Anderson, Melanson and Maly, 2007) suggested that behaviourally the board of directors were adopting a more collaborative approach that included closer ties with management; the opposite of what agency would predict. Additionally, the findings not only suggest higher prevalence of collaborative boards, but also a strong level of cognitive support among directors for the new model as most effective in carrying out the board’s fiduciary duties. These findings raised the question as to why directors would respond so and chart a course that seemed to challenge the orthodoxy of agency based reforms.

It has been posited that directors responded to post-Enron reform efforts with a search for a new model of practice that was efficacious to protect themselves from a heightened sense of liability (Anderson, Melanson and Maly, 2007). Given this, I predicted that directors would then have to enact practices if the new model is to be efficacious – couple adoption to the technical core of practice. The candidate model chosen by directors appears to be one advocated by the director professional association, the National Association of Corporate Directors (NACD), in a report on boards acting collaboratively with management as a strategic asset to the firm (NACD, 2001 – see also Appendix A). The report explicated a new model of practice that represented a collaborative role for the board in addition to their monitoring role consistent with the theoretical development of Sundaramurthy & Lewis (2003). Importantly, professional associations are a source of legitimation and dissemination of new practice within their constituency (Greenwood, Suddaby and Hinings, 2002) and so the NACD presented an alternative and legitimate model of practice for boards to consider.
Boards enacting practice as a strategic asset to the firm would represent a significant departure from prior assessments of boards being largely symbolic bodies where rhetoric and action are largely de-coupled from the actual core activities of the board (Westphal and Zajac, 2001; Westphal and Zajac, 1998; Zajac and Westphal, 1995; Judge and Zeithaml, 1992). Further, a board acting as a strategic asset to the firm would imply a board that could influence firm performance outcomes above and beyond reduction of agency costs by providing strategic counsel to management consistent with a stewardship approach (Kroll, Walters and Wright, 2008; Westphal, 1999, Davis, Schoorman and Donaldson, 1997).

While the board may adopt a model of practice consistent with the board acting as a strategic asset (collaborative model), issues arise as a consequence of this development with respect to the ability of the board to objectively monitor management. This is because a collaborative board will develop closer ties with management (Sundaramurthy and Lewis, 2003; Westphal, 1999, Davis, Schoorman and Donaldson, 1997) in conflict with agency prescribed board relations with management; arms-length and neutral (Eisenhardt, 1989). But it has been argued that collaborative boards must balance monitoring and collaboration to ensure enhanced organizational outcomes and this creates a tension that the board must continually manage (Sundaramurthy and Lewis, 2003). Still, it has also been reported that collaborative boards do not appear to be compromised in their ability to effectively monitor management (Westphal, 1999).

This thesis examines if collaborative boards are or are not compromised in their ability to monitor management but also, examine if collaborative boards may even have enhanced monitoring abilities that would support the practicality of directors adopting the collaborative
model as efficacious. It should be noted that this thesis does not attempt to determine if collaborative boards improve organizational performance outcomes as this is left for future research. It should also be noted that this thesis represents an exploratory phase in the research with respect to the institutional processes that might be driving the evolution of the board to a new model of practice. While I posit that the NACD, as a professional association, may have initiated the process via broadcasting (Greenwood, Hinings and Suddaby, 2002) the new model to its constituency, how the model diffused to become more prevalent is a question left to future research. I now discuss more specifically the research contributions

With respect to institutional theory, this research then contributes to theory by exploring the melding of ‘old’ institutionalism (efficacious models of practice) with the ‘new’ institutionalism (need for legitimacy) in the adoption of a new model of practice following a trigger or shock event – ‘Enron’(Greenwood & Hinings, 1996). ‘Enron’ represents a candidate triggering event for being a catalyst for institutional change (Melanson, Bates and Hennessey, 2003) in the face of perceived failures in the existing institutional arrangements with respect to the corporate board of directors and their oversight role in order to maintain well functioning capital markets. Lastly, this thesis is to my knowledge the first to capture transforming institutional change in corporate governance as it unfolds over time. The thesis is organized as follows. First a literature review of institutional theory followed by a review of key research in agency theory and corporate governance is provided to acquaint the reader with past empirical and theoretical work. After the literature review, theory and hypotheses follow that set up the key empirical tests. Data, methods and results follow the hypotheses and this in turn is followed by discussion of the results, research limitations, conclusions and avenues for future research.
Chapter Two

Institutional Theory
Two Schools of Thought: the “Old” and the “New” Institutionalism

Institutionalism as a theoretical framework is very broad with many strands that cross multiple disciplines including, but not entirely limited to, economics, political science and sociology. In addition, institutional theory and each of its strands has evolved considerably in its thinking since the early pioneers in the late nineteenth and early twentieth century. The theoretical evolution has been to such an extent that there is often a distinction made between the old and new institutionalism; new institutional economics and the new institutionalism in sociological research (Scott, 2008; Greenwood, Oliver, Sahlin and Suddaby, 2008). The old institutional perspective saw the institutionalization process as adding value above and beyond value from meeting technical requirements of tasks (Selznick, 1957). On the other hand, new institutionalism places emphasis on the symbolic nature of practices and structures that possess legitimacy as opposed to adoption for purely efficiency or value added reasons (Powell and DiMaggio, 1991). It should be noted the not all institutionalists agree with the demarcation, believing instead that the “new” institutionalism is largely a continuation of the “old” institutionalism; the similarities outweigh the dissimilarities (Selznick, 1996).

What follows is an overview of early institutionalism and its pioneers from which modern institutionalists draw inspiration. This is followed by a review of the new institutionalism with focus on sociological approaches and finally, discussion of institutional pressures and change processes and applications to corporate governance.
Early Institutional Theory and Evolution to the “New” Institutionalism

The foundations of the old institutionalism and their application to organizations (firms) were laid by Philip Selznick (1948) in which he describes the organization as a rational system that acts through its leadership and membership to achieve objectives in an efficient manner. Selznick draws inspiration from Weber’s views of social and economic organization (Weber, 1947 – essays 1920 to 1926) in which the society organizes itself in a manner to achieve greater efficiency such as the ‘protestant work ethic’ to achieve goals. Weber argued that the protestant work ethic was an institutionalized social construct based on innovations in religion that facilitated the rise of Europe as a centre for world domination in the nineteenth and early twentieth century (Weber, 1946).

Selznick, similarly to Weber, argues that routines and practices are institutionalized over time by adaptation to its external environment with intent to ensure organizational survival and success through greater efficiency (Selznick, 1948). The routines and practices represent specific ways of doing things that reduces uncertainty by constraining human behaviour and making it more predictable and in this way, has value to the firm. However, Selznick goes further by proposing that the institutionalization process develops a bonding fabric that defines the organization both in the present and its historical heritage that adds value above and beyond technical and efficiency gains (Selznick, 1957).

The social bonding and importance of historical heritage draw from early criticisms of economic thought by Thorstein Veblen whom ridiculed “the hedonistic conception of man as a lightning calculator of pleasures and pain” (Scott, 2008, citing Veblen, page 3). Veblen cited the
lack of consideration of man embedded in social structures and historical change in economic thought as unrealistic. Social structures evolve over time and actors within develop habits that are a reflection of history and interactions with other actors so habits become institutionalized and constrain behaviour (Veblen, 1919). The concept of habits constraining behaviour influenced not only the old institutionalism (routines and adaptation to reduce uncertainty; Selznick, 1948) but also the new institutionalism; taken for granted and the ‘iron cage’ whereby unwritten rules (habits, routines etc.) guide and constrain behaviour (DiMaggio & Powell, 1983).

With respect to social structures, they can be Weber’s protestant community or they can be organizations and firms as distinct entities for study (Selznick, 1957) or even organizational fields of practice that can cross many organizations (Greenwood, Oliver, Sahlin and Suddaby, 2008) that commonly possess professional associations (accounting and financial professions and corporate directors as a profession as examples) that pronounce what is legitimate practice within their fields (Greenwood, Suddaby and Hinings, 2002).

The concept of organizational fields also drew from, and perhaps more directly from, the pioneering writings of Berger and Luckmann (1967) that asserted ‘the social creation of reality’. This view asserts that reality is socially constructed based on human symbolic interpretations of rules and conventions that produce cognitive frameworks that define cognitive systems (Scott, 2008, on Berger and Luckmann, page 16). Berger and Luckman attempted to bridge earlier institutional thinking with new institutional thinking to lay the foundations for emergence of the "new" institutionalism in sociological scholarship (Scott, 2008).
Berger and Luckmann were highly influential in the development of the new institutionalism as their work implies the importance of cognitive processes in defining normative systems that flow from shared meaning systems and knowledge. This shared knowledge and meaning systems can be within an organization as a distinct entity for institutional study but may also be communities of knowledge shared across multiple firms such as organizational fields of practice; accounting, finance, corporate governance and the like. This laid not only foundations for conceptualization of organizational fields as entities for study (Greenwood & Hinings, 1996) but brings institutional thinking full circle to Max Weber’s concepts of social structures and communities of shared practices and beliefs. The new institutionalism employs multiple levels of analysis including the firm and social structures such as organizational fields but with emphasis on symbolic meaning, legitimacy and cognitive processes in institutionalization processes (Scott, 2008). While this emphasis may be more so than earlier institutionalists, some question whether it represents something novel enough to consider “new” (Selznick, 1996).

The old institutional thinking also placed importance on historical considerations in the construction of institutions and this influenced new institutionalists that examined institutional change processes to understand how institutions emerge, change and even de-institutionalize (Dacin, Goodstein & Scott, 2002; Greenwood & Hinings, 1996; Greenwood, Suddaby & Hinings, 2002; Hoffman, 1999; Townley, 2002). Further, Veblen (1919) cited the importance of human interactions in the institutionalization process that influenced later theorists in economics such as agency (Eisenhardt, 1989) and the new institutional economics (North, 1990). Importantly, later institutional theorists recognized the importance of agency in institutional
processes with respect to responses to institutional pressures (Oliver, 1991) and change agents acting to enact change in the institutional arrangements in structuration theory as a branch of institutional scholarship (Giddens, 1984). Thus, early institutional theorists laid the foundations for later thinking in institutionalism that has since branched out in many fruitful directions on how institutions emerge, are conserved, evolve over time and even de-institutionalize.

**Emergence of the “New” Institutional Theory**

The development of “new” institutionalism brings the organization into focus as a distinct entity for study (Scott, 2008) and also the concept of organizational fields that consist of shared meaning systems that define their boundaries (Greenwood, Oliver, Sahlin and Suddaby, 2008). The new institutionalism also asserts the importance of symbolic systems and the adoption of practices because they are deemed legitimate as a sociological phenomenon that shapes institutions as opposed to economic efficiency arguments (Scott, 2008). This is an important assertion as it implies that practices or structures deemed illegitimate would not necessarily be adopted even if deemed more efficient. And further, that practices and structures may also be adopted for legitimacy purposes even if sub-optimal. This view can then help explain why some institutional forms persist despite the options of more efficient forms (Meyer & Rowan, 1977).

However, the concept that inefficient institutional practices can arise and persist was influenced by the work of Robert Merton (1940) and his essay “Bureaucratic Structure and Personality” in which he argued that leaders of organizations could concern themselves so much with conforming to rules and conventions that it could run at cross-purposes to the goals of the organization. Merton also connected this conformity to symbolic values and legitimacy:
There may ensue, in particular vocations and in particular types of organization, the process of sanctification… through sentiment formation, emotional dependence upon bureaucratic symbols and status, and effective involvement in spheres of competence and authority, there develop prerogatives involving attitudes of moral legitimacy which are established as values in there own right, and are no longer viewed as merely technical means for expediting administration. (Merton, 1940, page 202)

Selznick, an influential institutional theorist largely associated with the “old” institutionalism built upon and was influenced by Robert Merton’s essays on bureaucracy:

Institutionalism is a process. It is something that happens to an organization over time, reflecting the organizations own distinctive history, the people that have been in it, the groups it embodies and the vested interests they have created, and the way it has adapted to the environment… In what is perhaps its most significant meaning, “to institutionalise” is to *infuse with value* beyond the technical requirements of the task at hand. (Selznick, 1957, pp 16-17, italics in original)

Selznick and Merton both make explicit that institutionalization is a process that occurs over time, meaning it is dynamic and institutionalization can be treated as a variable. Thus, the concept of institutional change was a part of the early thinking in the emergence of the new institutionalism despite the sentiment among scholars that the theory has primarily focused on why institutions look the same (isomorphism) rather than how they evolve and change (Dacin, Goodstein and Scott, 2002). Also, Selznick suggests a role for agency in the institutionalization process, taken further by one of his students, Stinchcombe (1968) that influenced later work on institutional change (structuration theory) and responses by actors to institutional pressures (Oliver, 1991).
It should be mentioned here that Selznick is sometimes referred to as part of the old institutionalism but Selznick himself argued that such demarcations between the old and the new institutionalism are overstated as there is more of a continuum of evolving development of the theory, then there is in two distinct branches (Selznick, 1996). Selznick pointed out that often expressed differences are not all that different or just reflect a shift in emphasis. For example:

The new institutionalism in organization theory and sociology comprises a rejection of rational-actor models, an interest in institutions as independent variables, a turn towards cognitive and cultural explanations, and an interest in properties of supra-individual units of analysis that cannot be reduced to aggregations or direct consequences of individuals’ attributes or motives. (Selznick, 1996, p. 273, quoting DiMaggio and Powell, 1991, p. 8)

In other words, Selznick saw the new institutionalism as more a shift in emphasis as opposed to something truly novel. Further, the work of Merton and Selznick, both influenced by earlier scholars such as Max Weber and Veblen, laid the foundations for examining institutions as an independent variable and questioning scholarly adherence to rational actor models due to value of ‘form’ above and beyond efficiency. Selznick does acknowledge the important contribution in the ‘new’ institutionalism of the cognitive and cultural component in institutional processes. While change agents are deemphasized, as opposed to their centrality in structuration theory, the role of individuals and interactions in aggregate are part of the “old” institutionalism such that the “new” institutionalism is not departing from the “old” but rather being perhaps narrower in approach. However, the cultural-cognitive component of new institutionalism actually lays the seeds for structuration theory and the role of individual agency.
While the new institutionalism places emphasis on legitimacy as an “imperative” to justify adoption of practices leading to isomorphism in the pursuit of having legitimate form, this is also a response to or adaptation to environmental uncertainty which is a topic explored and developed in the “old” institutionalism (Selznick, 1996) and analogous to Merton (1940) arguments on over-conforming and Selznick (1948) on routines and adaptation to reduce uncertainty. Routines and habits to reduce uncertainty (Selznick, 1957) arguably influenced “new” institutionalists such as DiMaggio and Powell’s (1983) work on isomorphism through mimetic processes to adopt practices from legitimate organizations to enhance survival in uncertain environments. Concluding with Selznick, to label as ‘new’ is questionable “from the standpoint of social science and social policy… most important, perhaps, is a failure to integrate the old and the new by taking full account of the theoretical and empirical continuities [of the “old” and the “new” institutionalism] (Selznick, 1996, p. 275).

Thus, while recognizing novel contributions of the “new” institutionalism, I have attempted here to explicate how institutional theory in general, through numerous examples, has evolved from early scholarship that influenced later scholarship in the development and elaboration of the theory over time. Hence, later scholars built upon and drew inspiration from the work of earlier scholars more so then embarking on a new theoretical framing. I now turn to the “new” institutionalism as a continuuation in theoretical development of institutional theory, noting that scholars recognized the continuity of themes and discussed this to bring convergence between the ‘old’ and the new and some labelled this convergence as “neo-institutionalism” (Greenwood and Hinings, 1996, p. 1023; Scott, 1994, pp 55-80).
“New” Institutional Theory

The new institutionalism came into the mainstream of organizational studies in the 1970’s with the work of Silverman (1971). Silverman criticized Selznick’s structural and functional views as being overly concerned with “stability, order and system maintenance” (Scott, 2008, p. 42) and drew more from Berger and Luckmann’s (1967) social construction of reality. While this approach does not dismiss the importance of regulatory and normative forces, it does shift emphasis to the importance of cultural and cognitive processes. However, stability, order and system maintenance are themes that are as much a part of the new institutionalism (DiMaggio and Powell, 1983, 1991) as they are in the old institutionalism (Selznick, 1948, 1957; Merton, 1940) albeit framed in slightly different semantics.

Two influential papers by Meyer and Rowan (1977) and Zucker (1977) further elaborated on Silverman (1971) and were also influenced by Berger and Luckmann (1967). Meyer and Rowan (1977) saw institutions as “complexes of cultural rules” that specify procedures to meet specific goals that effect the wider institutional environment and can diffuse such as through professional associations. While Meyer and Rowan (1977) developed the cultural ‘macroside’, Zucker (1977), a student of Meyer, placed emphasis on the cognitive belief systems that shape behaviour. Once institutionalized, cognitive beliefs construct objective reality as ‘fact’ and are transmissible (Zucker, 1977). Building upon the work of Meyer and Rowan’s cultural systems and Zucker’s cognitive systems, DiMaggio and Powell (1983) formally laid down mechanisms of institutionalization in the form of three ‘pillars’ of institutional processes.

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1 This would be a basis for diffusion of governance practices through director interlocks, for example, the poison pill (Davis, 1991)
The Three Pillars

The new institutionalism proposes multiple pillars of support for constructing a reality of what is legitimate action and structure (DiMaggio & Powell, 1983; Scott & Meyer, 1994). This framework asserts the importance of coercive rules, normative frameworks and cognitive frames in guiding, constraining, and empowering behaviour (Scott, 1995; DiMaggio & Powell, 1983; Scott & Meyer, 1994). Recently, the literature has come to refer to the third pillar as the cultural-cognitive pillar as opposed to just cognitive as recognition of how the external cultural environment can shape internal mental schema and cognitive interpretations (Scott, 2008) fusing Meyer and Rowans (1977) cultural systems and Zucker’s (1977) cognitive belief systems into a single pillar. The ‘pillars’ of support are provided in the table below:

< Insert Table 1a Here >

The first pillar, regulatory, comprises of rules and laws within some domain, typically national, although not necessarily so, such as international laws and treaties which are transnational in scope. Regulations are imposed by the state which possesses coercive powers over the society and enactment of laws confers legitimacy to conform or otherwise be illegal and subject to sanctions as defined by the state and its delegated institutions. Lack of conformity can be viewed as illegitimate but not always if the law or the state itself loses legitimacy.

While rules and laws may provide coercive legitimacy, organizational practices may also become legitimized over time because they are widespread in practice and may be adopted for the sake of perceived legitimacy through normative pressure rather than improved performance within their social environments (DiMaggio & Powell, 1983; Meyer & Rowan, 1977; Westphal,
With widespread adoption, these practices can become taken for granted within cognitive schema, representing the third pillar of support. This can even extend to the ‘bending’ of the law. For example, speed limits are the law but rarely followed, with the qualification that there is a relatively understood reasonable limit to how much the speed limit is exceeded. This is generally taken for granted in society and law enforcement officers rarely enforce the law if the speed limit is exceeded within the generally accepted norm.

In addition to the three pillars, institutional theorists sought to define social environments that set the boundaries of domains or communities of practice (Greenwood, Oliver, Sahlin and Suddaby, 2008). Social environments can also refer to organizational fields within which sets of organizations have established professional boundaries and shared meaning systems (DiMaggio & Powell, 1983; Greenwood, Suddaby & Hinings, 2002). Organizations within a field develop shared systems of meaning and ‘socially constructed reality’ through interactions with each other and it is this shared belief system that defines the boundaries of the field (Greenwood, Oliver, Sahlin and Suddaby, 2008; Scott, 1994). Institutional theorists have also grappled with how institutions arise, change and even disappear and this can also apply to organizational fields of practice; for organizational field, the role of professional associations has been of particular interest in institutional change processes (Greenwood, Suddaby & Hinings, 2002).

**Institutional Change**

Although institutional pressures can lead to change through increasing isomorphism, they can also lead to deinstitutionalization and the emergence of new structures (Dacin, et al., 2002), creating periods during which substantial variation may be observed as organizations seek to
understand what constitutes legitimate behaviour. In response to organizations within a field seeking direction on what is legitimate practice, organizational fields often develop professional associations to guide their respective fields on what is deemed best practice and acceptable as part of a professionalization process (Lounsbury, 2007). In this way, professional associations are an important source of normative guidance by proclaiming what is legitimate practice within their fields such that legitimate practice diffuses through their fields by mimetic processes (Greenwood, Suddaby & Hinings, 2002), and thereby increasing structural and behavioural isomorphism (DiMaggio & Powell, 1983).

Professional associations can serve to provide moral guidance on what is legitimate practice to help its constituents adopt practices deemed appropriate and proper (Greenwood, Suddaby & Hinings, 2002). For example, the scandals often referred collectively to as ‘Enron’ caused a crisis in the accounting profession leading to the Canadian Institute of Chartered Accountants (CICA)² to issue guidance on the separation of audit and consulting services among its members. While the guidance was voluntary, all major accounting firms adopted promptly the guidance from the CICA (Melanson, Bates and Hennessey, 2003). Professional associations can then be conduits for change processes by defining new practices or modifying new practices that confer immediate legitimacy to their field constituency (Scott, 2008). Institutional pressures can also become more acute and strengthened in response to significant disruptive events such that institutional change processes commence or accelerate; such events are referred to as ‘trigger’ events (Greenwood & Hinings, 1996) with ‘Enron’ being but one example (Melanson, Bates and Hennessey, 2003).

² The CICA is the primary association in Canada representing the accounting profession
Change processes can be characterized as convergent or radical (Greenwood & Hinings, 1996). Radical change is the abandonment of a template or ‘busting loose’ from an existing ‘orientation’ and the adoption of a new template. Convergent change is the ‘fine tuning’ or movement toward a particular template. An example of radical change is the adoption of strategic performance measurement systems in cultural institutions in the face of severe funding cuts (Townley, 2002). Such adoption meant discarding the dominant management forms of museums in Alberta and adopting new structures more in line with that seen in the private sector. Another example is the adoption of anti-takeover defences such as the poison pill or golden parachute (Davis & Greve, 1997), deemed radical at the time. In each case, organizational response was precipitated by a triggering event, which Greenwood and Hinings (1996) describe as ‘shock’ events that trigger substantive change. The emergence of the leveraged buyout as a disruptive innovation, for example, could be viewed as a triggering event for the adoption of the poison pill as a take-over defence, or a funding crisis in the case of cultural organizations in Alberta.

While these events have led to radical change, often from ‘perceived problems in performance levels or the perceived utility associated with institutional practices’ (Dacin, et al., 2002), events can also trigger convergent change resulting in increased isomorphism in practices (Greenwood & Hinings, 1996). Understanding why triggering events lead to radical or convergent change is an important problem for scholars of how institutional pressures act on organizational fields and ‘Enron’ as a candidate triggering event prompted my research program into potential institutional change processes it may have triggered with focus on the corporate board of directors.
Institutional Theory and the Corporate Board of Directors

Corporate governance has risen only relatively recently as a field of research in its own right. Research on corporate governance has been dominated by a legal-economic approach that largely views the firm as a ‘nexus of contracts’ and actors as self interested and self-serving and thereby, “has placed the principle-agency problems at the center of most researchers concerns and the result has been a rather narrow conception of corporate governance” (Greenwood, Oliver, Sahlin and Suddaby 2008, p. 389).³

However, corporate governance systems are embedded in an institutional environment that influences institutional logics that define legitimate action (Thornton & Ocasio, 2004). These logics reflect wider cultural beliefs and systems of rules that guide decision-making. Over time, logics can become so embedded and ‘axiomatic’ that ‘they come without saying’ (Greenwood, Oliver, Sahlin and Suddaby 2008). While legal frameworks can constrain actions due to threat of coercive sanctions, and given normative and cultural/cognitive factors, behaviours and actions of actors can vary within the context of governance systems. For example:

The board [of directors] has the authority to decide the boundaries of its active participation in relation to the responsibilities and goals it sets for management. Nonetheless, boards have acquiesced traditionally, permitting management to set the boundaries (Anderson, Melanson and Maly, 2007, pp 788-789).

Although the board of directors has ultimate authority in its oversight of the corporation, their power is often subordinated to management, which they are mandated to monitor and control. This leads to questions of why the board would not exercise their granted powers of

³ This is dealt with in depth in the chapter that follows
authority and control. The institutional tradition of studying organizations has from its early beginnings been concerned with issues of coordination and control which are common themes within the domain of corporate governance; “With its insights into the nature of authority and control systems, institutional theory is uniquely positioned to provide important contributions to scholarship on corporate governance” (Fiss P.C. in Greenwood, Oliver, Sahlin and Suddaby 2008, page 389). This is particularly so given the historical view of boards acquiescing to management despite being mandated to oversee management on the behalf of owners.

Given variation in how boards exercise and allocate power and resources within firms they oversee, boards and their systems of practices and behaviours are better understood by incorporating normative and cultural/cognitive aspects in addition to the economic/legalistic views of governance (rules and regulation). In this way, corporate governance models can be viewed from a wider perspective of cultural belief and rule systems that guide institutional logics of directors and how they may guide behaviours and decision making (Lounsbury, 2007). Over time, institutional logics that inform beliefs become embedded and taken for granted, that is, ‘they come without saying’ (Meyer and Rowan, 1977). Behaviours and practices can become taken for granted by directors even if they are counter to the legal and regulatory framework that guides the role and mandate of the board of directors (Greenwood, Oliver, Sahlin and Suddaby 2008).

Boards of directors do exhibit variation in practice and may be seen as a ‘continuum’ of practices that define the field (Greenwood, Oliver, Sahlin and Suddaby 2008). Further, practices can evolve through complex responses to institutional pressures, some of which are discussed at
length with respect to agency theory and governance reform efforts in the following chapter.

The board of directors as an organizational field in its own right is subject to normative pressures that can lead to mimetic processes of adoption to become legitimate (Greenwood, Oliver, Sahlin and Suddaby 2008). This however needs to be considered in the context of the existing and historical environment. In particular, how agency theory has played a key role in guiding reform efforts to change structure and practices of the corporate board of directors. I now provide a review of agency theory and its relevance to corporate governance. This is then followed by a more in-depth discussion of institutional theory and corporate governance under the chapter heading “Theory and Hypotheses”.
Chapter Three

Agency Theory & Corporate Governance
Separation of Ownership and Control

In Canada and other advanced capitalist economies the publicly traded corporation and the capital markets are key pillars of our economic system. Maintaining trust in public firms and the capital markets are important to their effective functioning and our economic well-being. Corporations have been around for centuries as the “body corporate”, dating to Queen Elizabeth I when the Spanish Company (1577) and the East India Company (1601) were formed (Daily, Dalton & Rajagopalan, 2003). However, unlike most large modern corporations, these early corporations were run by owner managers that had a large stake in the success or failure of the firms they ran. Today, most large public firms are run by management that have little to no ownership stake such that there exists a separation of ownership and control; shareholders entrust the running of the affairs of firms they have ownership in to a professional management team that act as their agents (Eisenhardt, 1989).

This principal and agent relationship has been the subject of extensive study and one of the earliest treatments of this development is the seminal work of Means (1931) in which it was observed: “Ownership of wealth without appreciable control, and control of wealth without appreciable ownership, appear to be the logical outcome of present corporate development” (Means, 1931: page 68). The agency problem that arises from separation of ownership and control provided fertile ground for agency theorists to study the principal and agent relationship in the context of widely held public firms and family run firms that are also traded publicly. Agency theory is rooted in economic theory that sees individuals as self interested and will act in ways that are self-serving (Fama, 1980). With control of firms in the hands of managers who act as agents on behalf of the shareholders, there exists a moral hazard in which the agents’ actions
may be opportunistic and not serving the best interests of the shareholders (Jenson & Meckling, 1976).

**Agency Theory and the Corporate Board of Directors**

Several bodies are in place to ensure the smooth functioning of the capital markets such as regulators, stock exchanges, professional associations and within firms – the corporate board of directors. The board of directors has ultimate authority over the affairs of the firm they oversee; the board’s primary roles include hiring, monitoring and firing of the CEO, approval of strategic plans, compensation plans and general oversight of the firm (Hansell, 2003). The board of directors use their authority to constrain management opportunism on behalf of shareholders. Solutions employed by the board of directors to constrain managerial opportunism combine a mix of monitoring and incentives. Monitoring is done to increase the amount of information available to shareholders about the behaviour of management while incentives serve to align the interests of management with that of the shareholders to encourage desired behaviour (Beatty & Zajac, 1994). Yet historically, boards of directors have tended to acquiesce to management, letting management run the affairs of the company largely unfettered (Anderson, Melanson & Maly, 2007; Hansell, 2003, Judge & Zeithaml, 1992).

Economists and agency theorists in particular argued that the solution for director acquiescence was to make boards more structurally independent of management such as the splitting of the CEO and board chair positions (Shleifer & Vishny, 1997; Eisenhardt, 1989). In this way, directors would act in a more independent manner without undue influence from management; e.g., make decisions in the best interests of shareholders rather then serving
management interests at the expense of shareholders (Westphal, 1998) and this would improve firm performance (Wright, Kroll and Elenkov, 2002). There is a rich debate within the literature on corporate governance and its efficacy. The debate follows two general streams: (1) improving the board’s monitoring capability through increased board independence from management by changes in board structure and process (Westphal, 1998; Sundaramurthy, Mahoney & Mahoney, 1997) and (2) improving incentives for top management to reward desired managerial behaviour (Matsumura & Shin, 2005; Stroh, Brett, Baumann & Reilly, 1996; Boyd, 1994; Tosi Jr. & Gomez-Mejia, 1989).

Also, a literature exists that examines incentives and board structure/process in combination (Frankforter, Berman & Jones, 2000; Westphal & Zajac, 1998; Beatty & Zajac, 1994; Zajac & Westphal, 1994). The attention to agency concepts in the academic literature attracted the attention of institutional investors that had built up a capacity for action and through large share holdings in firms, exerted pressures on boards of directors to adopt practices that would increase structural independence of the board (Monks, 2005; Useem, 1996). Agency theory also influenced regulators and for example, in Canada, the Toronto Stock Exchange released in 1994 a set of guidelines that were largely based on agency concepts of greater board independence. While the guidelines were not mandatory, listed firms were required to provide information in their proxy circular as to how the guidelines were being met or if not, why the guidelines were not being followed.

While the 1990s did see improvement in board structural independence (Westphal, 1998; and in Canada: Dey, 1999), investor groups argued it was not enough, that stronger regulation
was needed (Monks, 2001; Useem, 1996). Then the ‘Enron’ scandals occurred: As the new millennium dawned, a series of high profile corporate scandals shook the global capital markets and ‘Enron’ became a symbol to collectively represent what was perceived to be excessive executive greed and a systematic failure in corporate governance (Matsumura & Shin, 2005; Clarke, 2004).

Emboldened by the high profile failures, investor groups argued the scandals were a direct consequence of director failure to act independently of management in their oversight duties and allowing highly remunerated CEOs to destroy shareholder value (Anderson, Melanson & Maly, 2007; Matsumura & Shin, 2005). Consequently, ‘Enron’ triggered sweeping regulatory change in the United States through the passage in 2002 of the Sarbanes-Oxley Act (SOX). The effects of the passage of SOX were also felt in Canada since many Canadian firms are cross-listed on American exchanges thereby necessitating the following of SOX rules. The regulatory changes under SOX prescribed new mandatory requirements of the board including increased board structural independence – for example, board audit committees must be entirely composed of independent directors.

The argument behind the new regulations, in line with agency concepts, were that structural independence of the board would result in director conduct that is more independent of management (Monks, 2005). With greater director independence, directors would be more capable of exerting control over management through more engaged monitoring and designing incentives that better align management and shareholder interests, and from this would flow superior firm performance (Van den Berghe & Baelden, 2005; Zajac & Westphal, 1995).
Indeed, for directors of corporate boards, governance reform could be divided into pre-Enron and post-Enron, so fundamental the changes in the regulatory arrangements given SOX (Anderson, Melanson and Maly, 2007; Melanson, Bates and Hennessey, 2003).

**Agency Theory and Governance Reform; More Questions Than Answers**

With the academic literature largely dominated by agency theory, most policy on corporate governance reforms has been guided by agency concepts prescribing increased structural board independence and incentive alignment between management and shareholders as a way to solve the agency problem of separation of ownership and control (Kang and Zardkoohi, 2005; Matsumura & Shin, 2005). However, many past studies have failed to show a positive correlation between board structural independence and firm performance (Dalton, Daily, Certo and Roengpitya, 2003; Dalton, Certo, Roengpitya, 2003; Daily, Dalton & Rajagopalan, 2003; Daily, Dalton and Canella, 2003; Tosi, Werner, Katz and Gomez-Mejia 2000; Frankforter, Berman & Jones, 2000; Westphal, 1998). For example, Dalton, Daily, Certo and Roengpitya (2003) reported on a meta-analysis of 229 studies on financial performance and equity ownership:

...the results of our meta-analyses do not support agency theory’s proposed relationship between ownership and firm performance. This is a significant finding, as agency theory has been characterized as a theory of the ownership structure of the firm (e.g., Jensen & Meckling, 1976). Also, as we have noted, agency theory provides the theoretical foundation for the vast majority of research conducted in corporate governance (e.g., Shleifer & Vishny, 1997). Our results illustrate relatively low relationships between various categories of equity and multiple indicators of financial performance. (Dalton, Daily, Certo and Roengpitya, 2003, page 20)

If changes to board structure and processes actually do constrain opportunistic behaviour, and lead to better designed incentives to encourage desirable management behaviour, then this
should be reflected in the financial performance of the firm. That the results of empirical work on these questions are ambiguous has raised questions about agency theory, its general applicability as well as the efficacy of governance reform based on agency concepts. Agency theorists assume that board structural independence will induce independent director conduct, but does increased board structural independence actually lead to independent director conduct and more specifically, neutral and arms-length relations between directors and management?

The assumption in agency theory of conduct being guided by structure is to some extent conceptually rooted in the structure-conduct-performance paradigm of economic based industrial organization; performance is a function of conduct which is in turn a function of the industry's structure (Mason, 1939; Bain, 1956). However, this structuralist assumption of corporate director behaviour involves “great inferential leaps” in linking structure to outcomes (Forbes & Milliken, 1999). For example, it has been shown that while some boards adopted a more independent board structure, the structural changes did not necessarily bring about a substantive change in director behaviour; the change was more symbolic and lacking substance (Westphal & Zajac, 2001; Westphal & Zajac, 1998; Zajac & Westphal, 1995). Further, structural changes can also be neutralized by managerial responses such as flattery and ingratiating towards independent directors by the CEO; ‘board games’ (Westphal, 1998). How board structure guides conduct in practice has then been in and of itself a research question worthy of further study, especially in light of the direction of governance reforms premised on agency concepts post-Enron.

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4 With the understanding that it is recognized that conduct can effect structure and performance can also influence conduct and structure
Post-Enron, with a greater perception of director liability, boards are being subject to increased pressure to act independently and assert their monitoring authority over management and tie management pay more closely to firm performance (Matsumura & Shin, 2005); if so, director conduct could be more substantive and less symbolic. It was in this context that a collaborative research program with McKinsey was initiated within which I endeavoured to examine director and management attitudes and conduct that looked beyond board structural characteristics. While it is easier to observe and catalogue board structural variables, by themselves they may be insufficient to answer some research questions such as whether director conduct is truly independent – a construct that is not readily visible (Schmidt & Brauer, 2006). To get at director and management conduct and attitudes, survey methods were employed.

The Evolution of Corporate Governance

Recent published research using field research methods suggests that director attitudes and conduct has evolved in unanticipated ways (Anderson, Melanson & Maly, 2007). For example, it was found that while most directors have become more engaged and assertive in their monitoring role post-Enron, as is expected according to agency concepts, it was also found that most directors believe that a closer and more collaborative relationship with management is needed to effectively discharge their duties as opposed to a neutral and arms-length relationship. While an unexpected result, director responses indicated they believed that through closer working ties with management, they could be more effective in their monitoring role (Anderson, Melanson & Maly, 2007).
Agency theorists have argued that closer ties can undermine director independence (Westphal, 1998). However, a paper by Westphal (1999) found that a minority of boards acted collaboratively with management in providing strategic guidance and yet despite closer ties, the role of the board as monitor was not compromised. If independent directors have determined that a closer relationship with management is the best way to carry out their duties, then they are acting in a manner that they perceive is in the best interests of the shareholders, consistent with agency concepts. This is not without precedence. In a paper on the adoption of golden parachutes (Singh & Harianto, 1989) it was found that independent directors supported adoption of golden parachutes despite opposition from institutional investors that saw adoption of golden parachutes as rewarding managerial incompetence. However, independent directors saw management support of a takeover as necessary for its success and as takeovers often benefit shareholders, adoption could be seen as actually serving to align management and shareholder interests. With this understanding, adoption of parachutes by boards dominated by independent shareholders is consistent with agency theory. It can be argued similarly that if independent directors view closer ties as more effective for carrying out their monitoring role, then such attitudes and conduct among directors is also consistent with agency theory.

The agency assumption that neutral and arms-length relations with management is in the best interests of shareholders, like the assumption of structural independence producing independent conduct, represents another inferential leap. This assumption has been challenged in that closer board management ties can actually be beneficial: “social factors such as trust and perceived social obligations may promote rather than hinder board involvement and effectiveness in administering a firm” (Westphal, 1999, p. 7). Further, closer ties increase the
interactions between directors and management facilitating a greater exchange of information. One purpose of active monitoring is to uncover problems before they blow up into crisis (Daily, Dalton and Canella, 2003).

Prior research findings (Anderson, Melanson & Maly, 2007) suggest that the majority of directors see closer ties and collaboration with management as more effective in preventing crisis because directors perceive that they are more likely to uncover problems earlier through more frequent and deeper exchanges with management. Closer ties to management creates an appearance of a paradox in theoretical logic as agency theory asserts the need to minimize social ties to bolster independence and in so doing, improve organizational outcomes (Eisenhardt, 1989). But if directors believe closer ties as being in the best interests of shareholders, then this belief among directors would seem to resolve this paradox. While seen by most directors as more effective, closer board ties with management do carry risks should a board be unable to exert its authority over management when required (Anderson, Melanson and Maly, 2007). Close ties between the board and the CEO over time tends to lead to increased trust and a propensity for the board to overlook performance shortcomings of the CEO (Hambrick and Mason, 1984; Westphal, 1998). A collaborative board will likely develop closer ties with the CEO and may be less willing to act as discussed by this Canadian Board Chair:

“If you don’t trust the CEO, you should fire him. But as trust develops between board and management over time, we seem to be willing to give more leeway to a CEO. In these cases, after we let a CEO go, we often say it should have happened sooner.”

5 Quoted in; Anderson, Melanson & Maly, 2007, p. 790
Sundaramurthy and Lewis (2003) provided a framework in which both agency, control through monitoring and incentives, (Eisenhardt, 1989) and stewardship, collectivist and collaborative functions of the board (Davis, Schoorman and Donaldson, 1997; Fox & Hamilton, 1994), could be balanced such that one did not gain dominance over the other; excessive monitoring and independence may impede valuable information exchanges between the board and management and on the other hand, closer ties might lead to an inability to question management and act forcefully when necessary. Drawing from stewardship and agency theory, the authors assert that both collaborative and monitoring functions in balance are necessary for preventing organizational decline due to the board’s need for information yet at the same time a need to exert their authority over management when necessary (Sundaramurthy & Lewis, 2003). It is of interest to examine if collaborative boards that have developed closer ties to management can maintain a proper balance between their monitoring and service roles as seems to be asserted by directors in prior research (Anderson, Melanson & Maly, 2007).

Prior research also put forth a process model driving transformation of the board of directors towards a collaborative model and the model is repeated below to illustrate this proposed process.

< Insert Diagram 1 Here >

The research reported in this thesis represents a continuation of prior research to track the evolution of the board of directors to examine if transformation of the board is proceeding towards a collaborative model whereby the board acts as a strategic asset and if this new model is in the process of being institutionalized as a new means for boards to best carry out their duties. Towards that end, this thesis also examines if characteristics and practices consistent with
a board acting as a strategic asset are associated with director reports of their board being a strategic asset (enacted), representing coupling to the technical core as opposed to being symbolic.

To conclude, I have discussed in this chapter how agency theory has dominated the academic literature on corporate governance and how it influenced investors and regulators such that it has guided much of the governance reforms since the late 1980’s up until the present. However, I have also elucidated on how the theory has been poorly supported by empirical studies in attempting to test the efficacy of agency guided reforms. It is argued then in this thesis that following the high profile scandals at the turn of this century, directors searched for a new model of practice in governance that would prove more efficacious then practices dictated by agency concepts. The model adopted appears to be that of a stewardship model that attempts to balance monitoring of management with a collaborative partnership with management as the best way for directors to discharge their fiduciary duties as corporate directors.

The following chapter proposes hypotheses to test if the institutional transformation of the board is proceeding, being enacted and if the new model of governance is becoming embedded in the consciousness of directors and management as correct and proper. Lastly, hypotheses are proposed to evaluate the possible effects of board structural independence as well as closer board ties with management on board monitoring and incentive alignment in management pay.
Chapter Four

Theory and Hypotheses
Institutional Change and Corporate Governance Reform

As discussed above (Chapter 2), the corporate board of directors is arguably a well-established organizational field that possesses well understood practices that shape norms and cultural-cognitive belief systems of directors (Greenwood, Oliver, Sahlin and Suddaby 2008; Scott, 2008, Chapter 15). These norms and cognitive beliefs can act to constrain director action and attitudes and impede the adoption of new practices (Sanders & Tuschke, 2007). While directors may resist change, institutional theory does provide insight into institutional processes leading to change (Townley, 2002; Greenwood & Hinings, 1996). These change processes include the adoption as well as the abandonment of institutional practices in response to institutional pressures (DiMaggio & Powell, 1983; Oliver, 1991).

However, it is important to understand that practices do not diffuse into a blank template, but instead into an existing regulative, normative and cultural/cognitive framework that influences successful versus unsuccessful (fad) adoption (Greenwood, Oliver, Sahlin and Suddaby 2008; Scott, 2008) and also mediates the manner in which adoption manifests; responses by actors in adoption may lead to modification of prescribed practices through compromise or negotiation with sources of pressures to adopt (Oliver, 1991) or even symbolic adoption only (Westphal & Zajac, 2001; Westphal & Zajac, 1998; Westphal, 1998; Zajac & Westphal, 1995). I now discuss sources of pressures for adoption of new practices in the context of corporate governance reform.
Adoption of Governance Practices

Pressures to adopt new practices can originate from regulative and normative systems (Scott, 2008) and in combination with social movements that can cause normative pressures that over time translate in passage of regulations that codify new practices into law (Greenwood, Oliver, Sahlin and Suddaby 2008). Further, social movements and legal frameworks can find added legitimacy through theorization that lends support and facilitates diffusion (Strang & Meyer, 1993). Corporate governance reform is an example of the role of social movements (shareholder rights), theorization (agency theory) and regulative forces (Sarbanes-Oxley) in the diffusion of corporate governance practices and their eventual widespread adoption (Greenwood, Oliver, Sahlin and Suddaby 2008).

Agency theorists influenced regulators and institutional investors such that they pressured firms to adopt greater board structural independence (Monks, 2005). While board independence became viewed in the 1990’s as best practice and boards did move towards greater structural independence (Westphal, 1998; Dey, 1998), research, as discussed above, has suggested that the adoption is in some cases symbolic (Westphal & Zajac, 2001; Westphal & Zajac, 1998; Westphal, 1998; Zajac & Westphal, 1995). For example, many structurally independent boards were found according to one study to have adopted best practice in compensation plans through public pronouncements to stockholders but in practice, did not vigorously apply them to management, rendering the adoption and announcement largely symbolic (Westphal & Zajac, 2001).
Independence in structure may not translate to independence in practice (conduct) as indicated in compensation matters and this may be attributed partly to findings that management has adapted to greater director independence through behavioural changes – ingratiation to outside directors to undermine director independence (Westphal, 1998) leading to pronouncements as a part of symbolic management of stockholders but not backed up by action (Westphal & Zajac, 1998; Zajac & Westphal, 1995).

Thus, even when new practices are adopted such as the split of the CEO and chair positions to increase board structural independence, claims by directors of acting with greater independence of management may be more espoused than enacted; change in structure and outward appearances of practice were adopted more for legitimacy purposes as a part of managing stockholder expectations and thus in reality was symbolic. Thus, boards of directors may adopt new forms to gain legitimacy, but normative values and cultural-cognitive beliefs of directors may be harder to change as they are embedded in well established institutional logics.

From an institutional standpoint, DiMaggio and Powell (1983) argued that actors in organizational fields develop an ‘iron cage’ that constrains action through institutionalization processes that “involves the process by which social processes, obligations, or actualities come to take on a rule like status in social thought and action” (Meyer & Rowan, 1977: page 341). Unwritten rules can constrain the actions of actors as effectively, or perhaps even more so than codified rules and these unwritten rules over time are taken for granted in the cognitive consciousness of actors that are difficult to change even when the external environment changes such as new laws and regulations that prescribe new structures and behaviours; behavioural
changes may take time to evolve to new expected norms and the evolutionary aspect of institutional change has not gone unnoticed even in the institutional economics literature:

The change [in payment practices] was taking place, however, within the old fundamental institutional setting which had evolved to deal satisfactorily with a slowly changing self-sufficient manor. It is not surprising that the customs of the manor yielded only very slowly in most cases. It was hard to change what had been sanctified by tradition and was the only impersonal law of the land (North & Thomas, 1973, p.38).

Thus the embedded behavioural norms and cognitive beliefs of directors acquiescing to management can render directors more vulnerable to management manipulation such as ingratiation, resulting in increased structural board independence being less effective. However, events of great significance occasionally occur that can trigger institutional upheaval and accelerate change (Greenwood & Hinings, 1996).

As discussed above (chapter 2), among the processes by which institutions change are major events that trigger or accelerate change (Dacin, Goodstein & Scott, 2002; Greenwood & Hinings, 1996). The debacle of high profile scandals put corporate governance reform into the spotlight and so through a combination of increased pressures from governance reformists and coercive regulation, ‘Enron’ acted as a trigger event for institutional change (Melanson, Bates, Hennessey, 2003). The direction of change has been towards greater board structural independence and it has been found that boards have become more structurally independent post-Enron (Canadian Spencer Stuart Board Index, 2002-2006; Korn & Ferry, 2002-2006). However, while boards are becoming more isomorphic as structurally independent, prior research suggests that directors are rejecting neutral and arms-length relations with management and instead are embracing a closer and more collaborative model of governance to guide their conduct.
In this way, while board structure has moved towards greater structural isomorphism, director conduct appears to be moving in a different, if not radical direction – collaborative boards rather than boards as primarily monitors of management. Thus, while ‘Enron’ has served to accelerate convergent change with respect to board structural characteristics (Melanson, Bates and Hennessey, 2003), at the level of director conduct, radical change may be occurring, potentially ushering the emergence of a new model of corporate governance and directors acting then as agents of change. Importantly, the template of a collaborative board was given legitimacy through a 2001 report by the leading professional association representing corporate directors in the United States; the National Association of Corporate Directors (NACD); see Appendix A.

**Role of Professional Associations in Diffusion (Normative Pillar and Mimicry)**

Professional associations play an important normative role in legitimizing practices in the field they oversee (Scott, 2008). Professional associations through dissemination of guidance to its membership are effective in shaping what is deemed best practice and indicating to its constituency what are appropriate new practices or changes in existing practice. Professional associations can also exert their influence across national boundaries such as international non-government organizations (INGO’s). While INGO’s cannot enact law, nonetheless, they exert considerable influence through normative pressures to propagate standards and principles of what is appropriate behaviour (Scott, 2008). Many directors of corporate boards are members of a professional association representing their interests; in the United States it is the NACD and in Canada it is the Institute of Corporate Directors (ICD). While Canadian directors follow

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6 Measures of board management ties were along the three dimensions of interpersonal interactions, communication flow and degree of collaboration.
guidance from the ICD, they also monitor guidance issued by the influential NACD. Directors Associations provide guidance that indicates what is appropriate and they have the moral legitimacy to direct change in governance practice. Directors can then adopt the new template as now a legitimate mode of conduct.

Specifically, the NACD released a Blue Ribbon report in 2001 that encouraged directors to transform their boards from primarily monitors of management into strategic assets to the firm (see Appendix A). The NACD releases their influential Blue Ribbon reports on an annual basis and they represent collaboration between governance experts in both Canada and the United States\(^7\), influencing both Canadian and U.S. governance practice (and even Anglo-Saxon governance regimes more broadly – see Anderson, Melanson and Maly, 2007). In the case of the 2001 report, the old practice was the role of board as monitor of management and the new role as strategic asset – collaborative with and empowering of management.

With respect to shareholder rights, institutional investors have not indicated strong opposition to collaborative boards (strategic asset) but they have largely supported regulatory changes that promotes board structural independence with the intent that independent structure will guide independent director conduct (Anderson, Melanson and Maly, 2007; Melanson, Bates and Hennessey, 2003). Thus, institutional pressures legitimize on the one hand the board as primarily a neutral and arms-length monitoring body (agency and regulation) and on the other hand, to an extent, legitimize the board as a strategic asset (NACD guidelines and stewardship theory).

\(^7\) For example, Dr. David Anderson, a governance expert in Canada, chaired the panel that developed the 2002 NACD Blue Ribbon Report.
Hypotheses: Is Institutionalization of a New Governance Model Occurring?

While prior work suggested that the board is evolving to a collaborative model and has broad support as the most efficacious role (Anderson, Melanson & Maly, 2007)\(^8\), will it remain true with the passage of time such that governance “structures and processes come to be taken for granted” as a consequence of institutionalization processes (Judge & Zeithaml, 1992, p.769)? Cognitive and normative values tend to lag regulated structural changes that can diminish the intended effects of reform as evidenced in studies of corporate governance changes in transition economies (Peng, 2003) and may also lead to symbolic behaviours despite the intentions of reforms (Westphal & Zajac, 2001; Westphal & Zajac, 1998; Westphal, 1998; Zajac & Westphal, 1995).

In periods of transition, institutional logics can have a dual character, comprising of the old and the new logics until the new logic takes hold and becomes dominant (Zucker, 1983) and finally taken for granted. Consider the practice of *in camera* sessions where directors met without the CEO; initially this was done with reluctance and trepidation as directors were concerned that the CEO would see this as hostile. However, within a few years, boards did not give this a second thought – the practice had become taken for granted.\(^9\) However, if changes have not become sufficiently embedded into the cognitive consciousness and values of directors such that they are taken for granted and if pressures for change dissipate, then it is possible that change could prove transitory (Scott, 2008; Scott & Meyer, 1994; Zucker, 1977) despite guidance from the NACD that boards should strive to become strategic assets to the firm.

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\(^8\) This research indicated that approximately 78% of directors that participated in the 2004/2005 director survey viewed the collaborative model as most effective.

\(^9\) Based on discussions with directors in numerous interviews from 2004-2006
Since ‘Enron’, the capital markets had by 2006 and 2007 largely recovered\textsuperscript{10} and interest in governance reform may once again have receded as investors focus on profits in a cycle of crisis to regulation and once again to complacency (Clarke, 2004). With investors focused on profits, directors might see a dropping off in pressures to substantively enact changes in governance conduct and so revert to ‘old ways’. Prior research (Anderson, Melanson & Maly, 2007) indicated that most directors viewed collaborative boards with a closer relationship with management as more effective, representing cultural-cognitive support for normative guidance from the NACD that boards become strategic assets to the firm.

However, from guidance provided by the NACD on boards as strategic assets, collaborative boards are expected to be more knowledgeable of and be more active and proactive in the affairs of the firm, particularly development of the firm’s strategy (NACD Blue Ribbon Report, 2001; see also Appendix A). This guidance on behaviour as a strategic asset represents routines in the form of roles such that the board acts as support to management in addition to the boards monitoring role. Thus routines specified by the NACD are the normative carriers for changes in director behaviour that is consistent with expectations of a board acting as a strategic asset (see also Table 1b: Institutional Pillars and Carriers).

Thus, for collaborative boards, new routines reflect expectations for directors that are higher and directors need to work harder given their new role. If pressures on boards have

\footnote{\textsuperscript{10} Note that the financial crisis occurred after the completion of data collection}
slackened, then possibly directors will slacken as well in their resolve to adopt behaviours consistent with a collaborative model of governance – board as strategic asset to the CEO. However, if the new collaborative model of the board as a strategic asset is indeed becoming widespread in practice and thereby institutionalizing, it is hypothesised:\(^{11}\)

\[\text{H1a} \quad \text{Directors will more likely report that the board is viewed by the CEO as a strategic asset rather than being viewed with neutrality.}\]

If directors are to be more collaborative with management, it can be expected that the number and intensity of interactions between directors and management will increase. It has been suggested that a consequence of increased interactions is increased risk that the board may lose its arms-length objectivity as monitors of management (Westphal, 1999; Westphal, 1998). However, prior research suggests that for the board to be effective as a strategic asset to management and the firm, effective collaboration requires collegial relations and greater openness of communication between management and the board of directors despite the risks of closer ties (Anderson, Melanson and Mali, 2007):

\[\ldots \text{directors believe board effectiveness will be enhanced as they develop greater collegial relations with management. Neutrality might be viewed as sufficient if governance is construed solely as oversight, but not so if governance entails being a strategic partner.}\]

\[\text{Consistent with this view of enhanced collegiality, directors stated a need for more open communication between directors and management. If directors and management are going to collaborate they need to develop a state of trust and respect that permits human relationships to grow}^{12}\]

Given these director views, it is hypothesized:

\(^{11}\) The terms collegial, openness of communication and collaboration are discussed under ‘Dependent Variables – Board/Management Ties’ in the Chapter: Data, Methods and Results, starting on page 56.

\(^{12}\) Anderson, Melanson and Mali, 2007, pages 779-780
H1b Directors will more likely report that communication flow between the board and management is open as opposed to being neutral in nature.

H1c Directors will more likely report that the board has a collegial relationship with the CEO as opposed to being neutral in nature.

If the institutionalization process is continuing to proceed, it is also expected that director reports at the cognitive level that the new model is more efficacious will remain strong despite the possibility of reduced pressures, representing the third pillar of support. Quoting Scott (1994): “It is useful, I believe, to recognize the presence and importance of both cognitive and normative elements in all institutional complexes. The strength and staying power of institutions can be attributed to their multiple sources of support.”13 Staying power requires not only normative adoption but also embeddedness of ‘values’ within the cognitive processes of actors within institutions such that they become taken for granted (Scott & Meyer, 1994). In this way, the relaxing of pressures will have little impact as directors will have internalized the collaborative model as the way boards should behave in practice and the dual logic character of institutional change evolves into a dominant logic; shift from board as primarily monitoring role to collaborative role. It is hypothesized:

H2a Directors will more likely report that the board seen as a strategic asset by the CEO is more effective than being viewed with neutrality.

Consistent with director views that openness of communication between the board and management and the need for collegial relations is a requirement for the board to be effective as a strategic asset (Anderson, Melanson and Mali, 2007), it is also hypothesized:

H2b Directors will more likely report that communication flow between the board and management is more effective if open as opposed to being neutral in nature.

H2c Directors will more likely report that a collegial relationship between the board and management is more effective than a neutral relationship.

Enactment (Mimicry) or Espoused: Director Involvement in the Affairs of the Firm

The 2001 NACD Blue Ribbon report outlined key activities undertaken by boards acting as strategic assets (see Appendix A). It is possible that director reports on the board’s relationship with management are largely symbolic that lack substance, representing more a public relations face to shareholders that directors are more engaged with management in their duties (Westphal & Zajac, 2001; Westphal & Zajac, 1998). If director reports of greater collaboration are more than symbolic, then director reports of greater collaboration should be associated with reports of greater board involvement in the affairs of the company; development of strategy (enactment). Involvement in strategy entails the board providing advice and input into management strategic proposals and may even involve the board co-developing strategy with management (Schmidt and Brauer, 2006; Forbes and Milligan, 1999; Judge and Zeithaml, 1992).

Legally, the board has ultimate authority over the firm and what it as a body may decide upon and what it may delegate to management to decide; Useem & Zelleke (2006) discuss some of the issues and challenges of defining the roles and boundaries of the board and management. Prior research (Anderson, Melanson & Maly, 2007) has suggested that directors are wary of micromanaging the affairs of the firm by becoming too involved in execution of strategy (operations), as this is seen as the domain of management. Further, the NACD 2001 report on
boards acting as a strategic asset only endorses greater board involvement in the firm’s strategy and not the firm’s operations (“Focus on strategic issues” – see Appendix A). As well, regular discussion among directors in an NACD supported director discussion board cautions against involvement in firm operations.\textsuperscript{14} Thus, the collaborative board is not expected to be involved in operations. Thus, if reports that boards are acting as strategic assets are substantive, it is then hypothesized:

\textbf{H3} \hspace{1em} The greater the board’s degree of collaboration as reported by directors, the more likely Director’s will report greater board involvement in the firm’s strategy.

If boards are evolving towards a collaborative model, it is expected that some boards will be in the process of evolving to a collaborative model but will not yet have reached this level of involvement in the firm. Essentially, for these boards, directors will see the collaborative model as most effective but will report the board has not gotten their yet. If so, it is expected that if directors do not report the board as collaborative but report such a role as most effective, then a corresponding difference should be observed between what is reported involvement of the board in the affairs of the company (strategy) versus what is reported as the most appropriate level of involvement of the board in the firm’s strategy; for reasons already discussed, it is not expected that this relationship will extend into firm operations. It is then hypothesized:

\textbf{H4} \hspace{1em} If directors report that the board should be more collaborative then what they report as the actual degree of collaboration, then it is expected that directors will also report that their board should be more involved in strategy development than what they report is actually the case.

\textsuperscript{14} “The topic of micromanagement comes up periodically in the Corporate Governance Forum, an online discussion group hosted by the National Association of Corporate Directors. In one recent set of posts (September 20 and 21, 2005), a director asked if a certain action (asking to see the weekly cash report) would be considered micromanagement. Peer directors writing in generally agreed that it would be, and advised the director not to make the request unless the company appeared to be in financial trouble.” Anderson \textit{et al}, 2007, p.795
Enactment (Mimicry) or Espoused: Efficacy Belief of Board Impact on Firm Performance

A study by McKinsey & Company (2002) indicated that 15% of investors viewed corporate governance as more important than the firm’s financial reporting on profit performance or growth potential. Their study also showed that 22% of investors are willing to pay on average a 19% percent premium for equity in a firm that is perceived to be well-governed as it is believed this will translate to better long-run performance. As discussed previously, Westphal (1999) suggested that closer board management ties can be beneficial in the administration of the firm and thus enhance performance. From the 2001 NACD Blue Ribbon report, the following characteristics related to efficacy were explicated, consistent of boards acting as a strategic asset:

- Performance-enhancing ideas
- Enhance decision-making with rigorous analyses
- Establish high, realistic standards of performance

Further, directors are more likely to collaborate with management if they also hold a belief in the efficacy of the board to have a substantial impact on firm performance and through director actions, enhance organizational outcomes (Kroll, Walters and Wright, 2008; Westphal, 1999). It is put forth that director reports of greater efficacy of the board on its impact on firm performance being associated with director reports of greater collaboration would suggest that collaboration is more substantive (enacted) then symbolic (espoused). It is then hypothesized:

H5 The greater the reported board’s impact on firm performance, the more collaborative the relationship between the board and management as reported by directors.
Enactment (Mimicry) or Espoused: Efficacy and Director Knowledge

Collaboration has been shown to be associated with greater director knowledge and expertise (Westphal, 1999). Prior research suggests that boards have become far more knowledgeable of the firms they oversee (Anderson, Melanson & Maly, 2007). The psychological literature on job performance has shown that job knowledge is important as a determinant of job performance (Campbell and Campbell, 1988) and bolstered job knowledge leads to enhanced efficacy beliefs (Bandura, 1991). Further, it was found that greater board knowledge was associated superior acquisition outcomes and increased board effectiveness as advisors to management (Kroll, Walters and Wright, 2008):

Agency-based studies of boards of directors address factors relevant to board vigilance with respect to the monitoring of senior managers. We argue that relying solely on director vigilance may be limiting because vigilance without relevant experience is unlikely to ensure board effectiveness. Our contention is that boards comprising vigilant directors, as well as directors with appropriate knowledge gained through experience, not only will be better monitors, but also more useful advisors to top managers… Consistent with our expectations, the empirical findings indicate that vigilant boards rich in appropriate experience are associated with superior acquisition outcomes.15

From the 2001 NACD Blue Ribbon report, the following characteristics related to board knowledge were explicated, consistent of boards acting as a strategic asset:

- Knows and understands the company’s business and competition
- Provides intelligent “capital”

Knowledge should then enhance the board’s ability to provide expert counsel and enhance collaboration and increase the likelihood of management’s receptiveness to increased

15 Kroll, Walters and Wright, 2008, from paper abstract, p. 363
collaboration. Director reports of greater board knowledge being associated with reports of
greater collaboration would suggest that collaboration is more substantive (enacted) then
symbolic (espoused). It is then hypothesized:

H6 The greater the board’s knowledge of the firm as reported by directors, the more
collaborative the relationship between the board and management.

**Modified Agency Assumptions: Closer ties and collaboration enhance monitoring and so are in the shareholder’s best interests**

While agency theorists have asserted that closer ties can reduce director independence,
Westphal (1999) argues that his findings suggest that collaborative boards that have developed
closer ties with management by providing strategic guidance and counsel do not necessarily have
less engagement and effectiveness in monitoring of management. In fact, Westphal (1999) has
argued that a neutral and arms length relationship between the board can undermine effective
monitoring and even firm performance. Further, Kroll, Walters and Wright (2008) found that
boards can have a significant impact on firm performance, finding that greater board knowledge
and board involvement in the affairs of the firm led to superior acquisition outcomes. This
suggests that boards can improve organizational outcomes through greater interactions with
management despite the risks that closer ties pose to director independence. Sundaramurthy and
Lewis (2003) added to the debate on collaboration versus monitoring by providing a framework
in which the boards roles as monitor of management and collaborative role as a service function
to management are both necessary and need to be in balance for there to be superior firm
performance and avoid organizational decline.
Although regulatory changes and investor pressures have pushed for greater board independence and more neutral and arms-length relations between directors and management (Monks, 2005; Matsumura & Shin, 2005), if independent directors have come to their own conclusion that a closer relationship with management is the most effective way to enhance their monitoring function and as such they perceive closer ties are then in the best interests of the shareholders, then this behaviour among directors would be consistent with agency concepts. With increased concerns among directors of their exposure to liabilities should they fail in their oversight duties, directors may act in their own interests and become agents of change to reduce risk to themselves even if it conflicts with prevailing notions of what is best practice in corporate governance.

This phenomenon, already discussed, regarding unexpected behaviour among independent directors has been documented in the work of Singh & Harianto (1989) with respect to the adoption of golden parachutes. Further, it has even been argued from a stakeholder perspective that golden parachutes serve the interests of not only shareholders but the society as a whole:

Golden parachutes ensure effective corporate governance that, in turn, preserves the firm’s value for all stakeholders. Boards of directors enter into parachute agreements to protect recently hired CEOs’ human capital during periods of financial uncertainty and, thus, potential takeover activity. From an ethics viewpoint, golden parachutes are valuable to all stakeholders because they encourage merger or acquisition in lieu of bankruptcy. (Evans and Hefner, 2009, page 65)

Given the importance of a successful M&A strategy to the firm’s prospects, adoption of parachutes are then arguably serving to align management and shareholder interests which is one of the important functions of the board according to agency concepts. Analogous to golden
parachutes, directors may see closer ties as a means to increase the frequency and importantly, the effectiveness of interactions and exchanges between themselves and management. This facilitates directors gaining a more complete and accurate picture of what is really going on in the firms they oversee (Anderson, Melanson and Maly, 2007) and so, directors with this view, cognizant of increased director liability, may reject the agency assumption that neutral and arms-length relations with management is in the best interests of shareholders, thus de-legitimizing agency theorization and legitimizing stewardship theorization in guiding conduct. Further, the 2001 NACD Blue Ribbon report identified characteristics of boards acting as strategic assets that indicated enhanced monitoring:

- Enhance decision-making with rigorous analyses
- Energize management by empowering them and holding them accountable

Of interest is the second bullet point above that directs boards acting as strategic asset to both empower management while holding them accountable (monitoring), consistent with the arguments of Sundaramurthy and Lewis (2003) that are supportive of a stewardship view of the role of the board so long as the board can balance its dual roles of monitoring and collaboration. Given that directors see closer ties with management as enhancing their monitoring evaluation role and that this is in the interests of shareholders, it is hypothesised that:

H7a The greater the report of more collegial interpersonal interactions between the board and management, the more engaged directors will be with management in performance of their monitoring duties with respect of evaluation of management.

H7b The greater the report of more openness in communication flow between the board and management, the more engaged directors will be with management in performance of their monitoring duties with respect of evaluation of management.
The greater the report of more collaboration between the board and management, the more engaged directors will be with management in the performance of their monitoring duties with respect of evaluation of management.

Board monitoring also involves setting and administrating executive pay (Hansell, 2003) and effective board monitoring should be associated with greater alignment of CEO pay and firm performance (Eisenhardt, 1989). The 2001 NACD Blue Ribbon report identified characteristics of boards acting as strategic assets that indicated the importance of incentive design to promote executive behaviour that enhances shareholder value:

- Link executive compensation to shareholder value

Of interest here is if boards acting as a strategic asset that in turn develop closer ties with management can then hold management accountable with respect to compensation. Studies of executive compensation and corporate governance have indicated that it is one of the functions of the board that is most difficult to actually execute whereby executive pay actually aligns with firm performance (Matsumura and Shin, 2005; Zajac and Westphal, 1995). As such, this is a good test of the ability of a collaborative board to balance monitoring and collaboration (Sundaramurthy and Lewis, 2003). Given that collaborative boards are more likely to develop closer ties with management and that directors see closer ties as enhancing their monitoring role, will it extend to their ability to ‘Link executive compensation to shareholder value’? If Sundaramurthy and Lewis (2003) are correct that it is possible to balance closer ties and monitoring, it is then hypothesised:

The greater the report of more collegial interpersonal interactions between the board and management, the more engaged directors will be with management in performance of their monitoring duties with respect to aligning CEO pay with performance.
H7e  The greater the report of more openness in communication flow between the board and management, the more engaged directors will be with management in performance of their monitoring duties with respect to aligning CEO pay with performance.

H7f  The greater the report of more collaboration between the board and management, the more engaged directors will be with management in the performance of their monitoring duties with respect to aligning CEO pay with performance.

The next chapter presents the data, methods and models by which the hypotheses are tested and then this is followed with the results of the model tests.
Chapter Five

Data, Methods and Results
Sample and Data Collection

Two data sets are used for analysis. The first data set was collected over the period fall 2004 to spring 2005 and methods for that study are described in detail elsewhere (Anderson, Melanson & Maly, 2007). In the 2004/05 study, the director (non-executive or executive) was the unit of analysis in that the studies purpose was to understand the “attitudes, opinion and behaviour of directors in their own right, based on the totality of their experience across all the boards they have served.” (Anderson, Melanson & Maly, 2007, p.784). A total of 372 Canadian directors responded to the survey; see Appendix C for a copy of the 2004/2005 Canadian Director Survey.

As with the prior study, the new study data set was drawn from Canadian firms that were a member of the TSX composite index in 2006; see Appendix B for a reproduction of the 2006/2007 Canadian Director and Executive Survey. At that time the index comprised of 274 publicly traded firms listed on the Toronto Stock Exchange. However, I excluded firms that were subsidiaries of a parent or affiliates on the composite as the boards of the parent and subsidiaries or affiliated companies had high overlap of directors that sat on both boards. Also excluded were firms that de-listed or subject to takeover or merger during the period of data collection and as a result, a total of 249 firms were eligible. The TSX composite index is comprised of firms that are selected by the exchange so that the index is a general representation of the Canadian economy; composite member firms are then diverse in their size (not just the largest firms), their age and industry.
The corporate secretaries of each TSX composite firm were sent in October of 2006 a participation package that invited members of the board and senior management to take part in the survey. The purpose of this approach was to obtain multiple raters on both the management and director sides to increase validity and to provide a more robust representation of the firm that would not be possible with single raters (Judge & Zeithaml, 1992; Westphal, 1999). When surveying the upper echelons of public firms, participation has tended to be low with response rates below 25% being common and above 40% rare (Westphal, 1999). To increase the likelihood of firm participation, each package included a cover letter that discussed how the current research was a continuation of prior research (including a summary of key findings of past research) and how the findings were of interest to directors and management of public firms. The study was also endorsed by the Institute of Corporate Directors (ICD) which is the professional association in Canada representing corporate directors and directors of non-profits. Follow up was made in two stages over the course of the year 2007 (spring and the fall). In all, 105 TSX Composite firms participated (42.2% of eligible firms) with a total of 365 completed surveys from directors and management (231 non-executive director and 134 management surveys – 98 of which were executive directors) for an average of 3.5 surveys from each participating firm (range 1-18 surveys). For firm level descriptive statistics see Table 2 below:

Firm level data such as performance, size and age were obtained using SEDAR which stores electronically Canadian public company filings including annual reports, financial statements and proxy circulars. Proxy circulars were used to obtain board characteristics such as

< Insert Table 2 Here >
CEO tenure and board size. To test for non-response bias, a Kolmogorov-Smirnov test (Siegal & Castelan, 1988) was employed to determine if there existed any significant differences in distribution across key variables between the respondent and non-respondent group – firms of the TSX composite that participated versus members of the composite that did not participate. The variables tested were firm size (by revenue, assets and market capitalization), age and performance (by EPS and ROA). No significant differences were found between the respondent and the non-respondent group on these variables suggesting that the response group is representative of the membership of the TSX composite in general. However, it was noted that respondent firms tended to be on average somewhat larger in market capitalization and assets than non-respondent firms. While the difference was insufficient to be significant, larger firms tend to be subjected to greater scrutiny by investors, regulators and analysts compared to smaller firms and thus, directors and executives of large firms may be more motivated to participate in a governance survey (Westphal, 1999).

The survey used represented an evolution over several years in which earlier versions of surveys were piloted and validated through pre-tests (Fowler, 1993) and post-survey face to face interviews to increase face validity (Patton, 1987), ensuring questions were interpreted and the meaning of responses were as intended. In this way the survey was refined, and ambiguous or poorly worded questions were improved and language made less biased. To further reduce the potential for bias (DeVellis, 1991), survey questions subject to analysis were located in varying positions in the survey.
Dependent Variables – Board/Management Ties

In Westphal’s paper (1999), it is discussed that boards, in addition to their monitoring function, can provide a second function representing a collaborative service role in the form of ‘expert advice and counsel’ to management. The following questions of executives were used by Westphal (1999, page 24) as measures of collaboration (used a 5 point likert scale):

1. To what extent do you solicit board assistance in the formulation of corporate strategy?
2. To what extent are outside directors a “sounding board” on strategic issues?
3. How often have directors provided advice and counsel in discussions outside of the board/committee meetings (by telephone or in person)? _____ times.

The following questions of executives were used by Westphal (1999, page 24) as measures of the relationship between executives and directors (friends or acquaintance):

1. How many of the outside directors would you consider to be acquaintances or friends
   a. Acquaintances but not friends: _____ (number of directors)
   b. Friends: _____ (number of directors)

In my research, a similar approach was employed to examine board and executive ties by using 3 measures; nature of interpersonal interactions, openness of communication and degree of collaboration, also using 5 point likert scales. Prior research conducted in 2004 and 2005 (Anderson, Melanson and Maly, 2007) suggested that directors believed that for boards to effectively collaborate with management, certain conditions had to be met. The conditions fell into three main themes; (1) a relationship between the board and management that is conducive to cooperation (collegiality), (2) communication between directors and management needed to be open as frequency of exchanges was not sufficient to be effective, (3) the CEO sees the board as
a strategic asset. Given this, questions were constructed to measure along these dimensions and were incorporated into each of the two survey instruments employed; the 2006/2007 survey and the 2004/2005 survey.

For interpersonal interactions, see Question 10 on the 2006/2007 Canadian director and executive survey (Appendix B) and question 27 on the 2004/2005 Canadian director survey (Appendix C). The interpersonal interaction measure indicates the degree of collegiality between management and the board as observed by directors. With respect to response bias due to terminology employed in the scale, “Very Collegial” would be associated with negative feelings on what is seen as best practice; neutral and arms-length relations, as prescribed by agency concepts. Survey respondents will be cognizant of the expectation of “Neutral” relations by investors and regulators (perhaps even a ‘get tough’ stance such as ‘tense’) and that “Very Collegial” relations would be frowned upon. Thus, the term “Very Collegial” would be associated with social undesirability and as such, may bias the responses towards the more desirable and accepted relationship of neutrality (Bengo, 2006; DeVellis, 1991). Thus, social desirability bias suggests the scale for the nature of interpersonal interactions represents a conservative test of the hypothesized relationship between the board and management which predicts collegiality.

For openness of communication, see Question 11 on the 2006/2007 Canadian director and executive survey (Appendix B) and question 28 on the 2004/2005 Canadian director survey (Appendix C). While boards may vary with respect to the quality of interpersonal interactions with management and in the frequency of interactions, this does not necessarily mean that
information flow between the board and management regarding the firm is open. Collegiality could be quite high and interactions frequent but the information flow may be largely superficial and of a social rather than business nature. The term “Very Open” implies that information flow between management and the board is of high quality and informative of the true state of affairs of the firm. This level of information flow can facilitate closer collaboration between management and board, but this is qualified as it may also be a reflection of a more engaged board’s need for information as part of its monitoring function.

Thus, collegial relations and openness of communication flow does not necessarily imply boards are collaborative as it can represent collegial and open communication between the board and management as part of the board’s monitoring function. This said, prior research (Anderson, Melanson and Maly, 2007) suggests that collaboration, to be effective, requires openness in communication and that collaboration and more open communication flow can strengthen ties between the board and management including increased collegiality; collaboration is likely to be more effective is information flow is open and the board and management are on good terms – collegial.

For degree of collaboration, see Question 14 on the 2006/2007 Canadian director and executive survey (Appendix B) and question 4 on the 2004/2005 Canadian director survey (Appendix C). For this question, it was decided to operationalize the collaboration construct with respect to how the CEO views the role of the board. While the question could have referred to the board’s role with respect to the firm or to management in general, how the CEO views the board was considered critical to boards actually acting as a strategic asset given the overall
crucial role the CEO plays in the firm (Finkelstein and Hambrick, 1996; Hambrick and Mason, 1984). The CEO also plays an important role in change processes as they tend to be conservative and adhere to the status quo although CEO succession can increase likelihood of changes to the status quo such as being open to collaboration with there board (Kratz and Moore, 2002; Hambrick, Geletkanycz and Frederickson, 1993). Further, the CEO can potentially act to alter intended outcomes of governance reform efforts, rendering changes in practices as largely symbolic (Westphal & Zajac, 2001; Westphal & Zajac, 1998; Westphal, 1998; Zajac & Westphal, 1995). Thus, if the board as strategic asset is to be effectively coupled to the technical core (enacted), it is argued here that the CEO viewing the board as a strategic asset is a critical condition for this to be so.

With respect to degree of collaboration, the board as strategic asset was a term used by the National Association of Corporate Directors (NACD) in their 2001 Blue Ribbon Report (see Appendix A). As the professional association for directors in the United States, its reports are widely disseminated and are influential. In prior research (Anderson, Melanson and Maly, 2007), interviews with directors indicated their ability to discern a collaborative board acting as a strategic asset versus being generally helpful. Further, the conceptualization of the role of the board as collaborative rather then as primarily a monitoring body represents a significant shift in thinking (Kaufman & Englander, 2005). Prior research (Anderson, Melanson & Maly, 2007) indicated that a number of directors considered the board acting as a strategic asset as being inappropriate, in that it can represent an intrusion into managements domain and may constrain management initiative. Thus, the board as strategic asset is not universally supported.
Given that collaboration likely requires openness of communication and a collegial relationship between the board and management (Anderson, Melanson and Maly, 2007); it was tested using an ordered logistic regression if greater openness of communication and a greater degree of collegiality was associated with greater collaboration. The results showed a very strong association (P<0.001) for collaboration with both openness in communication and collegiality; this strong association also held when tested with controls. To further test the measure of collaboration, other measures that were indicative of collaboration based on the NACD (2001) Blue Ribbon Report was used in the form of questions on director involvement in strategy, director knowledge and efficacy beliefs on the impact of the board on firm performance; see also Appendix A. These additional measures are used to validate the collaborative measure and, to test whether collaborative boards, as reported by directors and management, are also engaged in collaborative activities and possess characteristics of a collaborative board such as enhanced knowledge (Kroll, Walters and Wright, 2008; Westphal, 1999).

**Dependent Variables – Board Monitoring**

For testing the level of engagement of the board in fulfilling its monitoring functions of management, questions on the boards level of influence in the evaluation of the strategy of the firm and evaluation of the execution of the strategy as well as questions on the importance of and appropriateness of CEO compensation. Evaluation of management and executive compensation are important components of the board’s monitoring function (Hansell, 2003). The questions relating to board evaluation are provided in Appendix B (see question 19, part II). The dependent measure represents the aggregate value of the scores for actual board influence on
evaluation of management on Strategy/Direction and Execution/Outcome where the higher the value, the greater the board’s influence in evaluation (more vigorous monitoring).

From prior research (Anderson, Melanson & Maly, 2007), directors employ a number of firm performance measures to varying degrees and so for this research, I chose not to assume what metrics directors and executives attached the most importance. For this reason, the survey employed multiple metrics (For all compensation measures, see Appendix B, Q.26) and asked respondents to rate the importance of each measure in tying CEO pay to that measure. The scores on the degree to which CEO compensation actually reflected performance are aggregated on the three measures directors rated most highly in importance in tying to CEO compensation (these measures also had lower variation compared to other metrics). They being: “Specific performance goals set by the Board for the CEO”, “Growth in earnings per share” and “Return on invested capital (ROIC)”.

In case executives might differ from directors on what is most important, it was determined whether non-executive directors and executives concurred on what are the most important compensation metrics; results found no significant difference between the two groups. The dependent measure then represents the aggregate score of the three metrics on how the compensation measure “actually reflected performance”. A higher aggregate score would then represent greater alignment between CEO compensation and firm performance.
Models and Analysis

To evaluate if institutionalization of a new governance model is proceeding, published research data from 2004/2005 (Canadian data only, see Anderson, Melanson & Maly, 2007) is compared to new Canadian data collected (2006/2007) using similar questions. Unlike the 2004/2005 data, the 2006/2007 study attempted to obtain responses from the entire board and senior management teams of a firm and responses were in regard to the targeted firm as opposed to general director experience.\(^{16}\) Given the broad range of the number of raters for each participating firm (range 1-18), to reduce bias due to some firms being over-represented compared to others, the results for each firm were also aggregated and the median used such that each firm had one response for each survey question (un-aggregated data was also analysed).

Because the questions of interest to be compared represent ordinal scales, a Wilcoxon signed-rank test was employed as it is not assumed that the difference between two variables is interval and normally distributed, but it is assumed the difference is ordinal; a non-parametric alternative to the unmatched pair Student's t-test (Agresti & Finlay, 1997). While non-response rates for the questions of interest were generally low (range 0.9% to 7.6%), to deal with the possibility of non-response bias, sensitivity tests were carried out using each of the two extremes on the response scales used as well as the median to determine if results of tests for significance remained unchanged; each non-response was replaced with the high extreme response and this was repeated for the lowest extreme response and then the median response. The results were

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\(^{16}\) This represents a significant difference and as such, the reported prevalence in the 2004/2005 survey may not be directly comparable to the 2006/2007 survey results and this is discussed under research limitations. Nonetheless, the reporting of a prevalence of 40% of firms acting as a strategic asset strongly suggests that prevalence has increased substantively from the time of Westphal’s (1999) findings in which only a small minority of boards acted as such. Note that the reports on efficacy of the board as strategic asset is comparable between the two surveys.
not materially different and robust across use of all three response values for non-responses. Reported results are based on replacement of a non-response with the median response for the question. All analysis was carried out using Stata statistical software (v. 9.0).

If institutionalization of the new collaborative governance model is proceeding, directors should report that board-management interactions along the dimensions of interpersonal relations, communication and collaboration respectively should be increasingly collegial, open and collaborative (H1c, H1b and H1a). Director reports on the relationship between the board and management along the dimensions of interpersonal interactions, communication and degree of collaboration from the 2006/2007 survey is compared to director reports along the same dimensions from the 2004/2005 study using a Wilcoxon signed-rank test.

For the 2006/2007 survey, similar to the 2004/2005 survey, each question asked what they observed in the present as well as what they deemed as ‘most effective’. However, the 2004/2005 survey also asked for respondents to retrospectively report what they observed 5 years ago. This retrospective report would place the time period just prior to ‘Enron’ (1999/2000) which approximates the time period of Westphal’s 1999 study that reported only a small minority of boards acted as a sounding board for council and advice on the firm’s strategy – i.e. act as a strategic asset. Although retrospective self-reports are not as reliable as reports on the present state of affairs as they introduce potential for recall bias (Groves, Fowler, Couper, Lepkowski, Singer and Tourangeau, 2004), it is still valuable to compare director’s retrospective report on the prevalence of boards acting as strategic assets to what is reported in Westphal’s (1999) study as well as compare to prevalence in the present (2004/2005 and in 2006/2007). It
would be of interest to find that retrospective reports of prevalence of boards acting as strategic assets are consistent with Westphal’s (1999) findings that only a small minority of boards acted as a strategic asset. With respect to recall bias, bias can be in either direction; over-reporting prevalence or under-reporting prevalence of boards acting as a strategic asset. There is the possibility that any over or under reporting of the prevalence of boards acting as a strategic asset will be normally distributed and cancel each other out such that no bias one way or the other occurs. However, social desirability (or undesirability) can bias responses in one particular direction (Bengo, 2006). Given that the NACD 2001 report indicated the desirability of boards acting as strategic assets, it is possible that desirability will bias recall responses towards higher prevalence of boards acting as strategic assets; over-reporting bias would actually serve to render the test more conservative. To test for the possibility of bias, it was examined if director reports on degree of collaboration that is deemed as most efficacious correlated with director reports retrospectively on degree of collaboration. Although the correlation was positive, the result was not significant.

Notwithstanding concerns for recall bias, should retrospective reports on prevalence of boards acting as strategic assets be consistent with Westphal’s (1999) findings and that reported prevalence ‘now’ is significantly greater than a small minority of boards, then such findings would suggest that prevalence has increased and that mimetic adoption by boards of the NACD 2001 report may indeed be occurring.
Cultural/Cognitive Embeddedness

If institutionalization of the new collaborative governance model is proceeding such that the efficacy of the new model is becoming cognitively embedded, director reports from the 2006/2007 survey of what they deem as the most efficacious board-management ties (interpersonal interactions, communication and degree of collaboration) should hold steady or strengthen when compared to director reports from the 2004/2005 survey on what is deemed most efficacious (H2a, H2b and H2c). Director reports from the 2006/2007 survey on what is deemed as the most effective relationship between the board and management is compared to director reports from the 2004/2005 survey using a Wilcoxon signed-rank test. Support by directors for the concept of the board’s role as strategic asset as defined in the NACD 2001 report would suggest that there is cultural/cognitive support for adoption. The cultural/cognitive component is an important institutional pillar in the institutionalization process (Scott, 2008).

Board Involvement in the Affairs of the Firm – Strategy Formulation

To examine if director and management reports of greater collaboration are more than symbolic and are instead enacted, reports of collaboration are compared to reports of board involvement in the development of strategy (enactment): see question 19 (part I) from the 2006/2007 Canadian director and executive survey Appendix B.

The greater the board’s involvement, the greater the collaborative role of the board is to be expected (H3). If greater board involvement in the strategy of the firm is associated with greater collaboration, than this can be seen as evidence that suggests collaboration is being
enacted. For this analysis, an ordered logistic regression is employed as the dependent variable is ordinal: as it is not assumed that the dependent variable is interval and normally distributed, but it is assumed the scale is ordinal; a non-parametric alternative to the ordinary least squares regression (Agresti & Finlay, 1997). The main effect model test is given below:

\[ \text{Collab} = \beta_0 + \beta_1\text{Strat} \]

Where ‘Collab’ represents the collaboration score from 1 to 5 representing an ordinal scale from lower to higher level of collaboration between the board and the CEO as reported by respondents. ‘Strat’ represents the score from 1 to 5 representing an ordinal scale from lower to higher level of board involvement in regard to firm strategy as reported by respondents. Support for H3 should see a positive and significant coefficient for ‘Strat’. Further, the main effect results should remain robust for the full model with controls.

If directors do not report the board as currently a strategic asset (collaborative) but report such a role as most effective, it is tested if there is also a corresponding difference between what is the reported involvement of the board in the affairs of the company versus what is reported as the most effective level of involvement of the board in the affairs of the firm. It is expected that greater expectations for board collaboration should correspond to greater expectations on what is the appropriate involvement of the board relative to actual involvement in strategy. For this analysis, an ordered logistic regression is again employed as the dependent variable is ordinal. The main effect model tests are given below:

\[ \text{CollabDiff} = \beta_0 + \beta_1\text{StratDiff} \]
Where ‘CollabDiff’ represents the difference between the collaboration now score and the collaboration rated as most effective score; representing a 0 to 4 ordinal scale from lower to higher level of difference between actual and appropriate as reported by respondents. Note that if a respondent reports that the actual level of collaboration is greater than what the respondent deems as most effective, then this should correlate with that respondents report of what is the level of board involvement in strategy versus what ought to be the level; in such a case as this, appropriate level of involvement should be less involvement than what is actual.

‘StratDiff’ represents the difference between the level of involvement now score and the level seen as appropriate score (a 0 to 4 ordinal scale from lower to higher level of difference between actual and appropriate as reported by respondents). For this analysis, an ordered logistic regression is employed as the dependent variable is ordinal: as it is not assumed that the dependent variable is interval and normally distributed, but it is assumed the scale is ordinal; a non-parametric alternative to the ordinary least squares regression (Agresti & Finlay, 1997). Support for H4 should see a positive and significant coefficient for ‘StratDiff’. Further, the main effect results should remain robust for the full model with controls.

To evaluate if reports of the board’s impact on firm performance is associated with the board’s collaborative role (H5), question 5 on the board’s impact on firm performance is used from the 2006/2007 Canadian director. The main effect model is:

\[ Collab = \beta_0 + \beta_1 \text{BoardImpact} \]
‘BoardImpact’ represents the level of reported board impact on firm performance as a score; being a 1 to 5 ordinal scale from lower to higher level of board impact on firm performance as reported by respondents. For this analysis, an ordered logistic regression is employed as the dependent variable is ordinal: as it is not assumed that the dependent variable is interval and normally distributed, but it is assumed the scale is ordinal; a non-parametric alternative to the ordinary least squares regression (Agresti & Finlay, 1997). Support for H5 should see a positive and significant coefficient for ‘BoardImpact’. Further, the main effect results should remain robust for the full model with controls.

To evaluate if board knowledge enhances the board’s collaborative role (H6), the survey question on director knowledge of the risk factors faced by the firm is used. Managing organizational risk is viewed as a high priority by most managers and directors (Smallman, 1999) and directors in prior research have indicated that the board needs to balance downside risk with upside potential of decisions for optimal outcomes in the best interests of the firm (Anderson, Melanson and Maly, 2007). Thus, it is expected that an understanding of the risk profile of the firm is important for the board to effectively collaborate with management. Four areas of risk are considered; (1) Financial Risk, (2) Operational Risk, (3) Regulatory and Compliance Risk, and (4) Brand and Reputational Risk. Reports on the knowledge of the four areas of risk faced by the firm are added to form a single aggregate ordinal variable representing overall knowledge of the risk profile of the firm. Question 20 on the board’s risk knowledge from the 2006/2007 Canadian director survey is provided in Appendix B. The main effect model is:

\[ \text{Collab} = \beta_0 + \beta_1 \text{RiskKnow} \]
‘RiskKnow’ represents the reported level of knowledge of the board on the risk factors facing the firm; being a score from 4 to 20 as an ordinal scale from lower to higher level of knowledge as reported by respondents. For this analysis, an ordered logistic regression is employed as the dependent variable is ordinal: as it is not assumed that the dependent variable is interval and normally distributed, but it is assumed the scale is ordinal; a non-parametric alternative to the ordinary least squares regression (Agresti & Finlay, 1997). Support for H6 should see a positive and significant coefficient for ‘RiskKnow’. Further, the main effect results should remain robust for the full model with controls.

Do closer ties interfere or enhance the monitoring role of the board of directors?

Monitoring is measured using questions that inquire about levels of board influence in evaluation of management on strategy and execution (H7a, H7b and H7c) and how well CEO compensation relates to firm performance (H7d, H7e and H7f) – classic monitoring and control functions of the board (Hansell, 2003). The response scores to the questions on the levels of board involvement in evaluation of management on strategy and execution are added together to form a single ordinal measure of board monitoring with respect to evaluation. From the 2006/2007 Canadian director survey, question 19 (part II) asks directors to rate the board’s involvement in evaluation of management (actual director involvement is the measure of interest – see Appendix B).
For CEO compensation being reflective of firm performance, the scores on the degree to which CEO compensation actually reflected performance are aggregated on the three measures directors rated most highly in importance. They being: “Specific performance goals set by the Board for the CEO”, “Growth in earnings per share” and “Return on invested capital (ROIC)” (see above under ‘Dependent Variables – Board Monitoring, starting at page 75, see also Appendix B, Question 26). The main effect model tests are provided below:

(1) MonEval = \beta_0 + \beta_1\ Collaboration + \beta_2\ Communication + \beta_3\ Interpersonal

(2) MonComp = \beta_0 + \beta_1\ Collaboration + \beta_2\ Communication + \beta_3\ Interpersonal

‘MonEval’ represents the level of influence (engagement) of the board in the evaluation of management regarding strategy and execution; being a score from 2 to 10 as an ordinal scale from lower to higher level of engagement as reported by respondents. ‘MonComp’ represents the level of alignment of CEO pay to firm performance on three metrics; being a score from 3 to 15 as an ordinal scale from lower to higher level of alignment as reported by respondents. For this analysis, an ordered logistic regression is employed as the dependent variable is ordinal: as it is not assumed that the dependent variable is interval and normally distributed, but it is assumed the scale is ordinal; a non-parametric alternative to the ordinary least squares regression (Agresti & Finlay, 1997). The tests are carried out where monitoring first represents the level of board involvement in evaluation of strategy and execution. The models are repeated using a measure of the appropriateness of CEO compensation as the dependent variable. To support H7a, H7b and H7c, the coefficients for main effect equation (1) respectively should be positive and significant. Further, the main effect results should remain robust for the full model with controls. For H7d, H7e and H7f, the coefficients for main effect equation (2) respectively should be
positive and significant. Further, the main effect results should remain robust for the full model with controls.

Controls

The following controls are employed and this is followed by a discussion of each in turn:

- Management (executive director)
- Firm performance lagged one year (ROA)
- Firm leverage (long term debt divided by assets)
- Firm age in years
- Log Assets
- CEO Tenure (years)
- Interaction between CEO and director or manager tenure (Years)
- Chair of the Board independent (dummy variable)
- Firm is cross-listed on an exchange in the United States (dummy variable)
- Size of the board (number of directors on board)
- Firm has a dominant shareholder; >5% (dummy variable)
- Percent of board independent
- Directors required to hold shares as 50% of retainer or greater (dummy variable)
- Year of survey 2007 (dummy variable; 0=2006 and 1=2007)

While the survey instrument was posed to directors of public firms of the TSX composite, many directors that sit on boards are also part of management and are therefore not considered outside directors and not independent. Directors that are also part of management, commonly referred to as executive-directors, may respond differently to questions of interest such as what role they think is most efficacious. Management have been found to often symbolically manage governance reform efforts rather than adopt in practice (Westphal & Zajac,
2001; Westphal & Zajac, 1998; Westphal, 1998; Zajac & Westphal, 1995). I include a dummy variable to indicate if the respondent is a part of the firm’s management team to control for differences that may be seen between non-executive director reports and that of executive directors.

Financial performance of the firm may influence the degree of monitoring by the board as well as other aspects such as increased board involvement when firm performance is poor (Daily & Dalton 1994; Beatty & Zajac, 1994). Thus I control for firm performance by lagging 1 year the return on assets (EPS and 3 year trends did not show any material difference). Firm size and age can also influence governance attitudes as larger and older firms are associated with greater inertial forces that are resistant to changes to the status quo (Hannon & Freeman, 1984). Thus I control for size (log assets; market capitalization and revenues were also tested and results were not materially different) and age (log years). CEO tenure is controlled for as CEOs may increase power and influence over board members as their tenure increases (Westphal, 1998; Finkelstein & Hambrick, 1989). Further, a relatively new CEO can be associated with increased likelihood of change in the status quo and openness to new ideas and practices by those in the upper echelons of the firm (Hambrick, Geletkanycz and Frederickson, 1993). It is suggested that the longer a CEO is in tenure with a director, the more likely closer ties can develop between the CEO and a fellow director (Westphal, 1999). Thus I control for this by interacting CEO tenure and director tenure but also apply the same interaction to fellow executives.

Further to the influence of the CEO on the board (and fellow executives), separation of the board chair and CEO positions is seen as an important indicator of board independence as a
combined position is viewed as power and influence enhancing for the CEO that is also chair (Zajac & Westphal, 1995). Another indicator of board independence is the percentage of directors that are non-executive directors on the board. The use of CEO and chair split and percentage of the board that are non-executive directors as indicators of board structural independence is common in the literature (Schmidt & Brauer, 2006; Westphal, 1999; Daily & Dalton, 1994). However, I went further with respect to the board chair in what was required to meet the test of true independence. For an independent chair, I required that the chair had not been an executive of the firm for at least 2 years and had no affiliation with the firm such as compensation outside of director retainer and also not an employee of a firm that had any material relationship with the firm that might compromise the independence of the chair.\textsuperscript{17}

The size of a board can also play a role in director attitudes towards governance through increased likelihood of directors on the board that sit on other boards and so through interlocks, may facilitate a flow of new ideas and perspectives on governance issues (Davis, 1991). Many publicly traded firms in Canada are also cross-listed on an American exchange. Such firms are then subject to U.S. regulations such as Sarbanes-Oxley and as such, directors and managers of such firms may hold different views on governance issues compared to directors and managers of firms that are not cross-listed. It has been put forward by some researchers that director ownership of shares may “enhance the power and activism of outside directors” (Westphal, 1998, page 525) and so director requirements to hold shares in the company are controlled for. Another important structural variable is the presence of a major block-holder. A block-holder has a significant equity position in the firm that motivates the block-holder to actively monitor

\textsuperscript{17} This enhanced definition of independence is consistent with the Canadian Spencer Stuart Board Index guidelines. Spencer Stuart and Clarkson Centre for Business Ethics and Board Effectiveness, 2006
the firm or be involved in the affairs of the firm such as influencing firm strategy and in some ways may substitute for board monitoring and board involvement in the affairs of the firm (Daily, Dalton and Rajagopalan, 2003). Thus I control for this by including a dummy variable for block-holder if there exists a holder of 5% or more of the firm’s equity.

While the 2004/2005 study had a tight window of follow up, the 2006/2007 survey was less so. The 2004/2005 survey was implemented in the early fall of 2004 and follow-up completed by the early spring of 2005 representing approximately a six month time window. However, the 2006/2007 survey was implemented similarly in the early fall of 2006 but follow-up was primarily in the fall of 2007, representing a sixteen month time window. To control for the extended time window, I use a dummy variable in the ordered logistic regression models that indicates if the survey was answered in follow up in late 2007.
Results

Evidence for Institutionalization of a New Governance Model

H1a, H1b, H1c, H2a, H2b and H2c

The tables below provide results for the statistical tests comparing results of the 2004/05 study with the 2006/07 study on ties between the board and management along the dimensions of interpersonal interactions, openness of communication and degree of collaboration by the board with management as well as temporal dimensions of the past and present and also what is deemed to be most effective.

< Insert Tables 3, 4 and 5 Here >

Note: for the 2004/2005 data, n=372, for 2006/2007 data, aggregated by firm, n=105. For un-aggregated 2006/2007 data, n=365 and the results were not materially different between tests using aggregated and non-aggregated data.

The results support hypotheses H1a (Table 3) in that the collaborative model of the board acting as a strategic asset has increased in prevalence and significantly so. However, the nature of the communication between the board and management (H1b) has not significantly progressed towards greater openness (Table 4). While the descriptive statistics do indicate there has been movement towards more very open communication between the board and management, it is not statistically significant. Hypotheses H1c (Table 5) is supported as the results for interpersonal interactions indicate that collegiality remains highly prevalent and has according to the 2006/2007 results moved significantly further towards greater collegiality when compared to reports from 2004/2005.
While the prevalence reported for 1999/2000 (4%) was based on recollection of the state of affairs five years prior to the time the survey was taken, and this can introduce recall bias, it is notable that this prevalence is consistent with a published study at the time (Westphal, 1999). Further, there are no reasons known to the author as to why the reporting of prevalence might be under-reported such that actual prevalence was higher. However, there is potential for over-reporting given that directors reported a high level of support for the collaborative model (discussed in greater detail below) and it is sanctified as proper by their key professional association (NACD). That is, the recall could be subject to positive bias such that prevalence is inflated (Bengo, 2006) and as such, a social desirability bias would in this case render the test conservative. In conclusion, the recall reports are likely to be reasonable estimates of the prevalence of collaborative boards for that time period, consistent with published accounts (Westphal, 1999). The results support H1a, H1c, but do not support H1b.

With respect to institutionalization of the new collaborative governance model from the cognitive perspective of what directors deem is most effective with respect to board-management ties, the results show that director reports show high support of the board as a strategic asset, for openness of communication and for collegiality, having held steady from 2004/2005 to 2006/2007, supporting H2a, H2b and H2c. It is notable that the results also show that reports for what directors see as the current openness of communication and the current state of affairs with respect to whether the board is acting as a strategic asset, there is a significant difference between what is seen now and what is deemed most effective. By this it is meant that many directors have indicated that currently, their board is not as open or as collaborative as they think
is the most effective. This suggests that boards may evolve such that prevalence of openness of communication and boards acting as strategic assets will increase in future, assuming that director efficacy beliefs also hold with time.

With respect to the nature of interpersonal interactions, the current nature of interpersonal interactions reported by directors was not significantly different from the nature of interpersonal interactions directors reported as the most effective. However, it is notable that 90% of boards are reported to have a collegial (70%) or very collegial (20%) relationship with management while only 9% of directors reported a neutral interpersonal relationship between the board and management. This indicates that the great majority of boards have adopted a collegial relationship with management in practice and deem this as the most effective relationship. To summarize, the results provide support that the board is evolving towards a new collaborative model of governance, the graph below visualizes the increased board-management ties:

< Insert Graph 1 Here >

Board as Strategic Asset – Enacted (Mimicry) or Espoused (H3)

Ordered logistic regression on the reported degree of collaboration (the dependent variable) was regressed against the reported board involvement in strategy development.

< Insert Table 6a Here >

The results were significant and provide support for the hypothesis H3 in that greater collaboration is associated with greater board involvement in developing strategy; director
reports of boards acting as strategic assets were also found to be more engaged in strategy formulation. A separate regression was run with respect to a collaborative board’s involvement in firm operations and directors did not, as expected, report greater board involvement in the firm’s operations (results not shown). The results were robust when the full model with controls was run. These results support H3.

**Degree of Collaboration Now Versus What is Reported as Most Effective (H4)**

To evaluate H4, the difference between the collaboration deemed as most effective score and the score for reported current collaboration is regressed (ordered logistic) against the difference between reported board involvement in strategy deemed as most appropriate score and reported actual board involvement score in strategy and in operations/execution.

< Insert Table 7 Here >

The results were significant and provide support for the hypotheses that greater distance between reported collaboration and what is deemed most effective is associated with greater distance between current board involvement in developing strategy and what is deemed most appropriate. A separate regression was run with respect to operations and the results were not significant as expected (results not shown). The results were robust for the full model with controls and so H4 is supported.
Board Impact on Firm Performance and Degree of Collaboration (H5)

Ordered logistic regression on degree of collaboration – the dependent variable was regressed against the reported board impact on firm performance to determine if the board acting as a strategic asset was associated with reports of higher board impact on firm performance.

< Insert Table 6b Here >

The results are significant and provide support for hypothesis H5 in that reports of greater board impact on firm performance is associated with greater collaboration. The results were robust for the full model with controls. This is consistent with the 2001 NACD Blue Ribbon report that boards as strategic assets should provide “performance-enhancing ideas”. H5 is supported.

Board Knowledge and Degree of Collaboration (H6)

The reported degree of collaboration was regressed against the aggregated scores on board knowledge of the firm’s risk profile; the overall risk knowledge variable is comprised of total reported knowledge on four areas of risk: (1) Financial Risk, (2) Operational Risk, (3) Regulatory and Compliance Risk, and (4) Brand and Reputational Risk.

< Insert Table 6c Here >

The results are significant and provide support for hypothesis H6 in that greater board knowledge of the risk profile of the firm is associated with greater collaboration. The results
were robust for the full model with controls. This is consistent with the 2001 NACD Blue Ribbon report that boards as strategic assets; “Knows and understands the company’s business and competition”. H6 is supported.

Testing Modified Agency Assumptions; do closer ties enhance monitoring?

H7a, H7b, H7c, H7d, H7e and H7f

Ordered logistic regression on the aggregate scores on the reported level of board involvement in evaluating management on strategy and execution (the dependent variable) was regressed against reports of the board’s interactions with management in regard to interpersonal interactions, communication and degree of collaboration.

< Insert Table 8 Here >

With respect to openness of communication and degree of collaboration, results were significant and associated with greater monitoring. However it was not shown that monitoring (evaluation role) was significantly affected by the level of collegiality in the nature of interpersonal interactions between the board and management; however, agency would predict that greater collegiality would impair monitoring. This is consistent with the findings of Westphal (1999) where it was found that increased board ties with management did not impair the board’s monitoring function. This is also consistent with the 2001 NACD Blue Ribbon report that boards as strategic assets should “Energize management by empowering them and holding them accountable”. The results were robust when the model was run with controls. The results support H7b and H7c but do not support H7a.
For monitoring and executive compensation, ordered logistic regression on the aggregate scores on the reported level of appropriateness of CEO compensation on three key performance measures (the dependent variable) was regressed against the reports of the board’s interactions with management in regard to nature of interpersonal interactions, openness of communication and degree of collaboration; the overall compensation appropriateness variable is comprised of total reported alignment on three compensation metrics, they being: “Specific performance goals set by the Board for the CEO”, “Growth in earnings per share” and “Return on invested capital (ROIC).

The results show that monitoring (compensation appropriateness) in relationship to reports on interpersonal interactions and degree of collaboration were not significant. However, the greater the degree of openness of communication between the board and management was significantly associated with reports of a higher degree of alignment between CEO compensation and firm performance. The results were unchanged when the model was run with controls. The results support H7e, but do not support H7d or H7f.

Summary of Results of Hypotheses Tests

A summary of the results of the hypotheses tests are provided in the table below:

< Insert Table 9 Here >

< Insert Table 10 Here >
Results: Control Variables

For the ordered logistic regression model tests for association between reported degree of collaboration and director behaviours and characteristics that are consistent with a board acting as a strategic asset (H3, H5 and H6), five control variables were consistently significant in their effects; CEO tenure, Tenure interaction, Chair Independent, Block holder and percent of the Board Independent. Longer CEO tenure and the board chair being independent were associated with reports of a lesser degree of collaboration between the board and management. Longer periods of time the same director and same CEO were tenured at the firm, presence of a major block holder and the greater the percentage of outside directors were associated with reports of a greater degree of collaboration between the board and management. While longer CEO tenure was associated with less collaboration, this appears to be mitigated by longer tenure of directors with the same CEO, suggesting that time allows for the director and CEO to develop a more collaborative relationship.

For the ordered logistic regression model tests for association between reported degree of collaboration and board monitoring with respect to evaluation of management (H7a, H7b and H7c), three control variables were significant in their effects; Management, Block holder and survey year; all three controls were associated with reports of a lesser degree of monitoring with respect to the evaluation of management. Management tended to view board involvement in evaluation of their performance as less vigorous as that reported by outside directors. With respect to the presence of a major block holder, the results are consistent with literature on how large shareholders can substitute for board monitoring (Daily, Dalton and Rajagopalan, 2003). With respect to the year control variable, it is unclear why the variable was significant only in the
case of the model for board evaluation; the year control variable was not significant in any other model tests. However, the variable was just significant at the 0.05 level so it is possible it represents a type I error (accepting the hypotheses when not true due to random significance).

For the ordered logistic regression model tests for association between reported degree of collaboration and board monitoring with respect to appropriateness of executive compensation (H7d, H7d and H7f), five control variables were significant in their effects; management, independent chair, percent of board independent, firm age and firm size. Management and the percentage of outside directors were associated with reports of a lesser degree of compensation appropriateness. Larger firms, older firms and an independent chair were associated with reports of a greater degree of compensation appropriateness.
Chapter Six

Discussion, Limitations and Future Directions
Discussion

It was posited that directors might respond to post-Enron reform efforts with a search for a new model of practice that was efficacious to protect themselves from liability (Anderson, Melanson and Maly, 2007). Further, it was expected that directors would then have to enact practices if the new model is to be efficacious. Based on earlier research (Anderson, Melanson and Maly, 2007) the model that appeared to be selected by directors is one that was advocated in a 2001 report by the director professional association, the National Association of Corporate Directors. The report (NACD, 2001) described a new model of practice that represented a new collaborative role for the board in addition to their monitoring role. The findings prompted me to initiate a new research project to answer key research questions that flowed from these prior findings.

The key research questions were if, since the broadcasting of the new model through a report by the NACD, prevalence of the new model of practice had increased with time and if the adoption of the new model of board acting as strategic asset is associated with actual director conduct that is consistent with such a model of practice – coupling to the technical core. And further, it was of interest to examine if the board’s new role compromised or possibly enhanced the monitoring role. Boards enacting practice as a strategic asset to the firm represents a departure from prior views of boards as largely symbolic bodies where rhetoric and action are largely de-coupled from the actual core activities of the board (Westphal and Zajac, 2001; Westphal and Zajac, 1998; Zajac and Westphal, 1995; Judge and Zeithaml, 1992).
Boards adopting and enacting a model of practice also result in closer ties with management (Sundaramurthy and Lewis, 2003; Westphal, 1999, Davis, Schoorman and Donaldson, 1997) in conflict with agency prescribed board relations with management; arms-length and neutral (Eisenhardt, 1989). Agency theorists argue that closer ties will compromise the board’s ability to effectively monitor management (Eisenhardt, 1989). While a study by Westphal (1999) found collaborative boards were not compromised, this research examines if monitoring may even be enhanced. The results of the research suggest that prevalence of collaborative boards has increased significantly and that the model of practice is enacted. Further, results also suggest that collaborative boards are not compromised in their monitoring function and in some respects, monitoring is actually enhanced. I now provide below a more complete discussion of the research findings.

**Institutional transformation**

The results of this research suggest that the board of directors is continuing to undergo institutional transformation that was identified in earlier research (Anderson, Melanson and Maly, 2007) in which the board’s role is evolving towards a collaborative model of governance. The results lend support that corporate boards are rejecting neutral and arms length relations with management and instead are adopting a closer working relationship that includes increased collaboration, collegial relations and openness of communication. Further, directors continue to maintain strong beliefs that collaboration, openness of communication and collegiality are the most effective relationships between the board and management as opposed to neutral and arms-length relations.
This represents a shift in director behaviour and practice away from that which is prescribed by agency concepts (Eisenhardt, 1989), this despite agency being further legitimized through a hardening regulatory regime as evidenced by the passage of the rule heavy SOX (Monks, 2005). This shift would suggest the board is moving closer to a stewardship model of governance that attempts to balance monitoring of management while empowering and collaborating with management (Anderson, Melanson and Maly, 2007; Sundaramurthy and Lewis, 2003) as an alternative to agency based models of governance practice.

Results of Canadian director reports suggest prevalence of the collaborative model has increased from a small minority of boards to approximately 20% of boards in 2004/2005 and then to approximately 40% of boards in 2006/2007. In addition to reported higher prevalence of the collaborative model, the great majority of directors (approximately 78% of respondents) see a collaborative board as most efficacious and this has held steady for several years post-Enron (Anderson, Melanson and Maly, 2007). Given this, it could be posited that collaborative boards may well become the norm as collaborative boards are seen as most effective (proper and correct) representing cognitive support for the adoption of new practice (Scott, 2008). However this should be qualified as these results are also consistent with fads that may arise from transient institutional pressures (Clarke, 2004).

While it cannot be ruled out that collaborative boards are a fad and will in time fade away, the results as of yet do not indicate the collaborative model being a fad; prevalence has significantly increased and cognitive support for the model remains strong. Indeed, it is difficult to rule out a fad until a significant period of time has passed since fads can, in some cases, take a
decade or more to come and go such as was the case with the leveraged merger wave of the 1980s (Stearns and Allan, 1996).

This said, it is important to consider that the overall institutional environment of the board of directors in Canada still remains largely framed in agency terms supported by regulatory reforms in the United States (Monks, 2005) and further, “SOX was used in Canada as the basis for reform of Canadian requirements” (Spector, 2006, page 1). Thus, the focus of academic literature on agency with respect to what is best practice in corporate governance (Greenwood, Oliver, Sahlin and Suddaby, 2008; Anderson, Melanson and Maly, 2007; Melanson, Bates and Hennessey, 2003) supported by regulation premised on agency concepts, taken together represent powerful twin pillars of support (regulative and normative: Scott, 2008, Scott, 1995, Scott and Meyer, 1994) that confers a level of legitimacy that would be difficult to challenge (Sanders and Tuschke, 2007).

Yet cognitively, directors appear to be contesting the agency model of governance, turning to guidance from the NACD as an influential association representing directors and thereby a source of legitimacy for new practice (Greenwood, Suddaby and Hinings, 2002) along with a nascent academic literature supporting a collaborative model of governance based on stewardship theory that is consistent with the new NACD proposed model (NACD, 2001). This leads to the next discussion on how directors may have evolved their thinking sufficiently to challenge well established institutional logics in corporate governance.
Adoption of Institutionally Contested Organizational Practices

As already discussed in this thesis under theory and hypotheses, institutional practices are adopted, become widespread in practice and persist as taken for granted through multiple pillars of support: regulative, normative and cognitive (Scott, 2008; Scott and Meyer, 1994). However, change can occur that contests a well established and legitimized institutional orthodoxy:

An organization faces relatively little resistance to attempts to adopt practices that are consistent with the three pillars of legitimacy. Indeed, adoption of such practices aids in the further legitimization of the organization. Yet new practices do emerge that at the outset are institutionally contested and contravene one or more of the pillars of legitimacy. Early adopters run the risk of stigmatization if a practice is ultimately discredited ... How do such practices get adopted and diffused when the need for legitimacy would seem to work against adoption and diffusion? (Sanders and Tuschke, 2007, page 33)

In the case of agency theory, academia and regulation infused agency based practices in corporate governance with moral legitimacy and dominated to such a degree that it crowded out for the most part alternative models of practice (Greenwood, Oliver, Sahlin and Suddaby, 2008; Anderson, Melanson and Maly, 2007). As a result, boards of directors that tended to acquiesce to management in the oversight of the firm (Anderson, Melanson & Maly, 2007; Hansell, 2003, Judge & Zeithaml, 1992) were pressured to adopt agency based practices that increased board structural independence (Daily, Dalton and Canella, 2003). As a result of these pressures, boards became structurally more isomorphic (Westphal, 1998; Dey, 1999).

Based on agency concepts, increased board structural independence should better equip the board to constrain management opportunism and design incentives to reward management for desirable behaviour and in turn, this should lead to better financial performance of the firm (Eisenhardt, 1989). However, the academic literature struggled to show positive correlation
between board structural independence and firm performance (Dalton, Certo, Roengpitya, 2003; Daily, Dalton & Rajagopalan, 2003; Daily, Dalton and Canella, 2003; Tosi, Werner, Katz and Gomez-Mejia 2000; Frankforter, Berman & Jones, 2000; Westphal, 1998). The results of most empirical work on these questions were ambiguous or came away empty handed and this brought into question whether agency theory was effective in guiding corporate governance practice. Thus, the general applicability of agency theory as well as the efficacy of governance reform based on agency concepts was contested in the academic literature.

As noted by Sanders and Tuschke (2007), early adoption of alternative practice that challenges the existing orthodoxy presents the risk of being deemed illegitimate. However, it is put forth here that two sources of institutional pressures acted together to initiate change. One of these sources was ‘Enron’ which represented a series of high profile corporate scandals that shook the global capital markets and was seen partly as a consequence of a systematic failure in corporate governance (Matsumura & Shin, 2005; Clarke, 2004; Melanson, Bates and Hennessey, 2003). As noted by Greenwood and Hinings (1996), powerful disruptive events in the institutional environment can trigger substantive pressures for change, even radical change. While Enron triggered convergent change in board structural practice (Melanson, Bates and Hennesey, 2003) despite the fact that Enron had an exemplary board with respect to its structure, ironically, it appears that Enron may have contributed to radical behavioural changes at the cognitive level of directors (Anderson, Melanson and Maly, 2007).

A previously published process model (see Diagram 1) posited that directors responded to Enron with some degree of fear due to an “increased perception of liability (e.g., legal,
reputational) resulting in steps to provide self-protection” (Anderson, Melanson and Maly, 2007, page 788; see also Clarke, 2004). Thus, with fear of liability, directors may have begun a search for new forms of practice that might prove more efficacious and serve to give directors more protection. This returns us to the old institutionalism of Selznick (1948) who argued that routines and practices become institutionalized over time as a result of adaptation to its external environment to ensure organizational survival and success through greater efficiency. Director awareness of increased liability meant that board practices had to work and given that the old orthodoxy was arguably wanting in regards to its efficacy\(^{18}\), directors needed to adapt to the new post-Enron environment; but how?

Adoption of new practices can be enhanced by sources of legitimacy that can be pointed too by adopters to defend their practices as morally correct (Greenwood, Oliver, Sahlin and Suddaby, 2008). One source, already discussed in this thesis, is that of the professional association (Scott, 2008: Greenwood, Suddaby and Hinings, 2002). The publishing of the NACD Blue Ribbon report in 2001 that endorsed boards acting as strategic assets to the firm conferred moral legitimacy to a new model of practice and communicated this to its constituency even though it contested the prevailing orthodoxy. This allowed directors that adopted early the ability to point to the NACD report as legitimating the newly adopted model of practice.

Another source of legitimacy is academic theory that validates and supports alternative models of practice. While stewardship theory is far less prevalent in the academic literature

\(^{18}\) While regulators and investors follow the academic literature, directors may be less inclined. However, directors were concerned about liability and searched for an effective response, aware that current best practice may not be sufficient – current practice being largely premised on agency concepts. However, many boards have members that are drawn from academia and they would follow the literature and be aware of the shortcomings of agency in the literature and could pass this on to their board. However, future research is needed to explore this more rigorously.
compared to agency, it has managed to be published in reputable academic journals (Kroll, Walters and Wright, 2008; Sundaramurthy and Lewis, 2003; Westphal, 1999; Davis, Schoorman and Donaldson, 1997; Fox and Hamilton, 1994) providing some level of normative support. It is noteworthy that the NACD report provides guidelines that follow closely a stewardship model of governance that combines collaboration with the boards monitoring role. Thus, although speculative, the academic literature on stewardship may have influenced the NACD decision to provide guidance to directors that boards can be effective as strategic assets and this in turn provided significant normative support for the new collaborative model of practice.

With the collaborative model of practice presented with normative sources of legitimacy and with director search leading to the conclusion that “the board [is seen] as most effective when viewed by the CEO as a strategic asset to management” (Anderson, Melanson and Maly, 2007, page 784) representing support from the cognitive pillar, the collaborative model could then draw upon two pillars of support. The question remains, what of the regulative pillar and the new model of governance practice?

The regulatory pillar, while largely framed in agency terms, does not specifically forbade collaboration and as such, boards that are structurally independent may still adopt a collaborative model and be legitimate. This means that collaborative boards that are structurally independent can draw from multiple sources of support (normative and cognitive) while not being inconsistent with regulatory requirements. This is consistent with literature on independent boards adopting practices deemed ‘effective’ and in the shareholders interests such as the ‘golden parachute’ (Evans and Hefner, 2009; Singh and Hariant, 1989) that were not prohibited
by regulation but were still deemed highly controversial. Thus, with multiple sources of support and regulation permissive of the new model, this together enhances the possibility of widespread adoption (Scott and Meyer, 1994) and institutionalization of the new model.

It is also noteworthy that cognitive support likely flows from director search for a new efficient model of practice as an adaptation to changes in the institutional environment (Anderson, Melanson and Maly, 2007) that is consistent with the old institutionalism (Selznick, 1948) yet the support is drawn largely from the cognitive pillar that is more associated with the new institutionalism (Scott, 2008). The research findings also lend support to the importance of individual agency in institutional change and together illustrate the interconnectedness of the old and the new institutionalism in explaining complex institutional change processes consistent with Selznick (1996) and Greenwood and Hinings (1996). This then effectively brings “together the old and the new institutionalism” (Greenwood and Hinings, 1996) in explaining radical institutional change as a search for practice that is both an efficient adaptation to the environment (Selznick, 1948) and yet has some level of moral legitimacy within its institutional environment (DiMaggio and Powell, 1983).

It then logically follows that the new model of practice, if it is to be efficient, cannot be decoupled from the technical core as has been the case in some responses to governance reform efforts (Westphal and Zajac, 2001; Westphal and Zajac, 1998; Tosi and Gomez-Mejia, 1989). It would then be predicted that board practices will mimic the model in practice as opposed to only symbolic adoption. This leads to the next discussion on the research findings that tested for enactment versus symbolic adoption.
Institutional Mimicry: Enactment versus Espoused – Coupling to the Technical Core

Based on guidance from the NACD on boards acting as strategic assets, degree of collaboration is expected to be associated with greater board influence in the development of the firm’s strategy but not the firm’s operations as this would be seen as micro-managing the firm. The results were as predicted and significant, lending support to the enactment of NACD guidance as opposed to symbolic adoption.

As a further test for enactment, reports of the degree of collaboration of the board versus what is deemed most effective are contrasted with reports of board involvement in the strategy versus what is deemed most effective. Results showed a positive correlation between director reports of a need for greater collaboration and reports of a need for increased board influence in strategy. This was an important test since the desirability for greater collaboration represents cognitive support for the collaborative model and the cognitive pillar can result in pressures (Scott, 2008) for greater involvement by the board in the firm’s strategy. The link between desirability for greater collaboration between the board and management and greater board involvement in the firm’s strategy suggests that boards that are not collaborative may evolve to collaborative boards. Given the majority of directors see the collaborative model as most efficacious, these findings lend support to the possibility of the collaborative model evolving to be the norm through widespread practice.

Also supported were tests of association between director reports of the board’s impact on firm performance and reports of the level of board knowledge of the risk profile of the firm with reports of the degree of collaboration between the board and management. It is unlikely
that directors would take the trouble to collaborate with management if they did not feel that their efforts would have any impact on the firm’s performance and this is also consistent with director beliefs of the efficacy of the collaborative model (Anderson, Melanson and Maly, 2007). Further, for boards to collaborate, knowledge of the firm is likely to enhance the effectiveness of collaboration which is consistent with studies on the impact of director knowledge on collaboration (Kroll, Walters and Wright, 2008, Westphal, 1999, Fox and Hamilton, 1994).

In summary, the association of director reports of increased board collaboration with management with greater board involvement in strategy, greater director knowledge of the firm and enhanced efficacy on the impact of the board on firm performance altogether suggest that collaboration is enacted as opposed to being merely espoused and symbolic; the enactment represents coupling to the technical core of board practice. Further, the association of director reports for the need for a greater degree of collaboration with director reports of a need for greater involvement of the board in the strategy of the firm lends further support and suggests a source of pressure on non-collaborative boards to transform to collaborative boards: noting that the prevalence of collaborative boards has increased from a small minority to nearly half of boards.

However, while most directors report that they support the collaborative model as most effective, management support is also an important consideration given that prior studies have shown management can act in some cases to render new board practices as more symbolic (Westphal and Zajac, 1998) or undermine the purpose of new practices (Westphal, 1998). To determine if management were as supportive of the collaborative model as non-executive
directors, a Wilcoxon test was employed and it was found that no significant difference in support between management and non-executive directors existed suggesting that cognitive support was statistically equally strong among management as it was for non-executive directors. However, the findings did indicate that longer CEO tenure was associated with decreased levels of collaboration between the board and management. This finding is consistent with literature on CEO commitment to the status quo and resistance to change whereby the likelihood of openness to substantive change, such as a move to a collaborative model, would be enhanced by succession to a new CEO (Kratz and Moore, 2002; Hambrick, Geletkanycz and Frederickson, 1993; Tushman, Virany and Romanelli, 1987).

On the other-hand, collaboration was enhanced by increased time that directors and a CEO were tenured together at the firm which could act to counter CEO resistance to change. This is also consistent with the literature on board and CEO ties where longer working relationships tend to result in a closer working relationship (Anderson, Melanson and Maly, 2007; Westphal, 1999) and further, cognitive frames between a board and a CEO tend to become a reflection of each other over time (Hambrick and Mason, 1984). Given that board ties with management strengthen over time through a closer working relationship with management, consistent with a collaborative model of governance (Davis, Schoorman and Donaldson, 1997), will the board be capable of balancing its monitoring function with collaboration (Sundaramurthy and Lewis, 2003)? I now turn to a discussion of the research findings relevant to this important question.
Impact of the Collaborative Model on Board Monitoring

A high prevalence of collaborative boards represents a significant change from the findings of past studies that found only a small minority of boards acted collaboratively with management (Westphal, 1999) and this is all the more striking given that regulation has pressured boards to become more structurally independent with the intent that directors will act more independently – neutral and arms length relations (Matsumura & Shin, 2005). Instead of neutral and arms-length relations with management, directors have developed closer ties and a more integrated working relationship with management that is more consistent with stewardship theory (Sundaramurthy & Lewis, 2003). One concern to agency theorists is that closer ties to management could undermine independent action of management to the detriment of shareholders (Eisenhardt, 1989). Given that directors have reported the model to be efficacious (improve board decision making) and that it may enhance the board’s monitoring role (Anderson, Melanson and Maly, 2007; Kroll, Walters and Wright, 2008; Kaufman and Englander, 2005; Westphal, 1999), this research examined this and I now turn to a discussion of the research findings.

Impact of the Collaborative Model on Board Monitoring: Evaluation of Management

At issue is the possibility that closer ties will gain an upper hand over the board’s balancing act of monitoring and collaboration (Sundaramurthy & Lewis, 2003) and undermine the monitoring function of the board. The results provide support for the assertion that the collaborative model enhances the board’s monitoring role with respect to board evaluation of management. Collaboration and communication were shown to enhance board evaluation of
management performance with respect to strategy formulation and execution. Further, collegiality was not found to compromise the board’s evaluation role, consistent with the findings of Westphal (1999):

Results showed not only that social ties fail to reduce the level of board monitoring activity, but also that such ties enhance the provision of advice and counsel from outside directors on strategic issues. (Westphal, 1999, pp 24-25)

And in prior published research:

Neutrality might be viewed as sufficient if governance is construed solely as oversight, but not so if governance entails being a strategic partner. Consistent with this view of enhanced collegiality, directors stated a need for more open communication between directors and management. If directors and management are going to collaborate they need to develop a state of trust and respect that permits human relationships to grow.” (Anderson, Melanson and Maly, 2007, page 790).

Thus, communication and collegiality are seen by directors as consistent with effective collaboration. Openness of communication facilitates directors obtaining a true picture from management of the firm’s state of affairs while collegiality promotes greater likelihood of open exchanges between management and directors (Kroll, Walters and Wright, 2008; Anderson, Melanson and Maly, 2007; Sundaramurthy & Lewis, 2003; Westphal, 1999). And while seemingly the reverse of what agency theorists would assert, directors report enhanced evaluation of management given that, as part of the boards’ collaborative effort “Open communication and frequent collegial interactions between management and a knowledgeable board can result in a higher likelihood of directors getting a clearer picture of what is going on from management.” (Anderson, Melanson and Maly, 2007, page 790).

It is also notable that the findings show the presence of a block holder is associated with reports of a lower degree of board evaluation of management which is consistent in the literature
where a block holder can to some extent substitute for board monitoring (Daily, Dalton and Rajagopalan, 2003; Stapleton, 1996). In conclusion and inconsistent with agency predictions (Van den Berghe and Baelden, 2005; Eisenhardt, 1989) but consistent with Westphal (1999), collegial relations do not necessarily impair the board’s ability to evaluate management performance and further, the collaborative model can actually enhance board evaluation.

**Impact of the Collaborative Model on Board Monitoring: CEO Compensation**

Literature suggests that directors and institutional investors hold the belief that the CEO has a large impact on firm performance (Anderson, Melanson and Maly, 2007; Hartzell & Starks, 2003). If so, it follows that what a CEO does matters and from agency theory it is important then for the CEO to have the right incentives to improve firm performance for the benefit of the shareholders (Monks, 1998; Eisenhardt, 1989). However, for effectiveness of aligning CEO pay and firm performance, it was found that only openness of communication had a substantive positive impact with degree of collaboration and collegiality having no significant effect. Compensation has been an ongoing issue with shareholders concerned that executives are rewarded disproportionately to the performance they deliver (Core and Guay, 2005; Matsumura & Shin, 2005; Financial Economists Roundtable, 2003; Hartzell and Starks, 2003). While collaboration and collegiality did not undermine this aspect of monitoring, they also did not enhance from these findings but notably, openness of communication had a significant positive effect.
Openness of communication may be effective as it can facilitate increased understanding between the board and management on the performance objectives by which management will be measured and how compensation will be affected. It has been found that compensation packages have become increasingly complex and difficult to understand and metrics employed also more complex (Matsumura & Shin, 2005; Core and Guay, 2005; Bernhardt, 1999). Thus, it is possible that open communication may enhance understanding between the board and management on director expectations of management and on how management will be evaluated. This in turn increases the likelihood of management delivering according to what is expected of them by directors.
Conclusions and Implications

From this research, it can be concluded that prevalence of collaborative boards (strategic assets) have significantly increased post-Enron and that the great majority of directors and senior management support cognitively this new model of practice (representing the third pillar of support). Further, the NACD as a professional association has endorsed the collaborative model of practice through official published guidance (a Blue Ribbon Report) that provided normative support for adoption (representing the second pillar of support). Lastly, the regulative pillar does not prohibit collaborative boards per se, with the focus being on the board being structurally independent with the assumption that conduct will follow accordingly. I conclude then that the new model of practice has institutional support that may be sufficient such that a new model of governance practice will institutionalize over time through wide-spread adoption and become taken for granted.

Another conclusion drawn from the results and theorizing is that director search for practices that would better protect them from liability post-Enron, suggests that adoption must be enacted and thus, connected to the technical core. This need for efficiency and the need for legitimacy bring together the old and the new institutionalism where in the face of a shock event there is a need for both efficacy and legitimacy for adoption of practices that contest the prevailing orthodoxy. This research also captures institutional changes as they are occurring, providing insights into institutional change processes and their complex nature. Another contribution is that this research lends support to a scant literature (Westphal, 1999) that closer ties between the board and management does not necessarily impair the board’s monitoring role.
Consistent with Westphal (1999), my results did not show that collaboration between the board and management interferes with the board’s monitoring function and in fact, results suggest enhancement of the monitoring ability of the board. Importantly, openness of communication appears to enhance alignment of CEO compensation and firm performance. Lastly, the results are not inconsistent with agency concepts in that non-executive directors believe that by developing closer ties with management, they are acting in the best interests of shareholders; and if monitoring is indeed enhanced, then rightly so.

What is also important here is the assumption of independent board structure guiding conduct that is neutral and arms-length between management and the board and that this is in the best interests of shareholders. In light of this research and consistent with literature questioning agency conceptualization of the agency problem in corporate governance (Dalton, Certo, Roengpitya, 2003; Daily, Dalton & Rajagopalan, 2003; Daily, Dalton and Canella, 2003; Tosi, Werner, Katz and Gomez-Mejia 2000; Frankforter, Berman & Jones, 2000; Westphal, 1999; Westphal, 1998), the assumptions that neutral and arms-length relations with management are in the best interests of shareholders needs to be changed. Also, given that boards are increasingly structurally independent, yet at the same time, prevalence of collaborative boards has increased, it is questionable that structural independence necessarily leads to neutral and arms-length relations between the board and management.

To conclude, the key implications of this research are that it adds theoretically by suggesting that an agency and stewardship model of corporate governance combined may be institutionalizing as a more effective model than a purely agency premised model of practice.
Further, this thesis has practical implications since regulators and investors need to be cognizant that their zealous application of agency based reform efforts may be not only sub-optimal, but in the end, harmful to the effective functioning of our capital markets.

Limitations and Future Research Directions

This research program, while suggesting that the board is evolving to a new model of practice, it is by no means definitive as it may also represent a fad that will come and go. This research is unique in that it is studying institutional transformation prospectively rather than retrospectively. Therefore, unlike studies that benefit from hindsight through study many years after the institutional changes have taken hold and institutionalized (Hoffman, 2001; Hoffman, 1999), this study does not have the benefit of hindsight and so it cannot be definitively determined whether the change is fad or a new institutionalizing model of practice. Thus, further research is needed to continue tracking the evolution of the new governance model to verify if the model is indeed institutionalizing or instead, is only a fad.

Prior research studied several Anglo-Saxon countries that are British offshoots (Anderson, Melanson & Maly, 2007) which did find generalizability of results for the countries under study, but the 2006/2007 study only examined Canada. Thus, it is not known if these results can be extended to other nation-states. Further, caution is advised with respect to the generalizability of findings since even though Anglo-Saxon countries tend to have similar governance practices (Stapledon, 1996), in developing and transitioning economies, very different governance practices and a substantially different institutional environment exists (Keasey, Thompson and Wright, 2005). Thus, future research is needed to explore if the findings
here are occurring in other countries and if the new governance model is taking hold with the
caveat that it needs to be appreciated the significant differences between the advanced economies
versus those that are developing or transitioning from command to market based.

This research has not rigorously examined the institutional processes that have driven the
evolution towards a new model of governance practice. While this thesis suggests that the
NACD diffused the new model by broadcast, it is unclear how diffusion actually manifests over
time. It is quite possible that the release of the NACD Blue Ribbon Report (2001) provided the
initial ‘infection’ and diffusion then proceeded virally through director interlocks. Further
research and tests of director interlocks with the existing data in needed to delve into such
questions. However, the ability to definitively answer the question on what processes are driving
the evolution is limited by the fact that the research is based on surveys unlike the studies of
adoption of poison pills and golden parachutes that are discussed explicitly in corporate
communications such as proxy circulars. Collaborative board practices are not so clearly or
explicitly discussed in corporate communications and this places limits on the ability to discern
the precise processes driving evolution to a new model of practice in this particular context.

Lastly, this research has not attempted to explore if collaborative boards are associated
with superior firm performance. Future research is required over time and this is viewed as
appropriate. This is because collaborative boards provide a service role primarily on the
strategic level and it can be years before performance effects of decisions of a strategic nature
become apparent. Thus, future research tracking collaborative boards would be more likely to
answer the question of performance effects of the new collaborative model.
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**Diagram 1**


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**Strategic Engagement Cycle**

**A. External Catalyst**
Corporate scandals (e.g., Enron)

**B. Response by key actors**
- Regulators: enact tighter controls; Investors: intensify scrutiny

**C. Initial director response**
- Fear: increased perception of liability (e.g., legal, reputational) resulting in steps to provide self-protection
- Enhanced preparation
- More probing questions

**D. Director adaptation**
- Increased engagement in governance role
- Collaborating with management
- Fuller analysis and discussion among directors and with management
- Richer understanding of the company and its environment
- Efficiency of board processes
- Meeting management
- Use of consent agenda

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1 **Response by key actors**
- Regulators: promoted director independence to clearly differentiate the governance function of the board by enacting tighter controls on director and executive behaviour
- Investors: intensified their scrutiny of board and corporate behaviour; pressed directors through targeted communication to display greater independence in exercising oversight; began taking concerted and efforts to develop and promulgate their expectations for director behaviour

2 **Initial director response**
- Directors felt their collective reputation was damaged; experience intensive media scrutiny for the first time; sense of collective siege on all sides

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# Table 1a

## Three Pillars of Institutions

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<tr>
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<th>Regulative</th>
<th>Normative</th>
<th>Cultural-Cognitive</th>
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<tbody>
<tr>
<td><strong>Basis of compliance</strong></td>
<td>Expedience</td>
<td>Social Obligation</td>
<td>Taken for grantedness, Shared</td>
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<td></td>
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<td>Understanding</td>
</tr>
<tr>
<td><strong>Basis for Order</strong></td>
<td>Regulative Rules</td>
<td>Binding</td>
<td>Constitutive Schema</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Expectations</td>
<td></td>
</tr>
<tr>
<td><strong>Mechanisms</strong></td>
<td>Coercive</td>
<td>Normative</td>
<td>Mimetic</td>
</tr>
<tr>
<td><strong>Logic</strong></td>
<td>Instrumentality</td>
<td>Appropriateness</td>
<td>Orthodoxy</td>
</tr>
<tr>
<td><strong>Indicators</strong></td>
<td>Rules, laws,</td>
<td>Certification,</td>
<td>Common beliefs, Shared Logics of</td>
</tr>
<tr>
<td></td>
<td>sanctions</td>
<td>accreditation</td>
<td>action, isomorphism</td>
</tr>
<tr>
<td><strong>Affect</strong></td>
<td>Fear Guilt/Innocence</td>
<td>Shame/Honour</td>
<td>Certainty/Confusion</td>
</tr>
<tr>
<td><strong>Basis of legitimacy</strong></td>
<td>Legally sanctioned</td>
<td>Morally governed</td>
<td>Comprehensible, Recognizable, Culturally supported</td>
</tr>
</tbody>
</table>

### Table 1b

**Institutional Pillars and Carriers**

<table>
<thead>
<tr>
<th></th>
<th>Regulative</th>
<th>Normative</th>
<th>Cultural-Cognitive</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Symbolic Systems</strong></td>
<td>Rules and Laws</td>
<td>Values, Expectations</td>
<td>Categories, Typifications, Schema</td>
</tr>
<tr>
<td><strong>Relational Systems</strong></td>
<td>Governance Systems, Power Systems</td>
<td>Regimes, Authority Systems</td>
<td>Structural isomorphism, Identities</td>
</tr>
<tr>
<td><strong>Routines</strong></td>
<td>Protocols, Standard Operating Procedures</td>
<td>Jobs, Roles, Obedience to Duty</td>
<td>Scripts</td>
</tr>
<tr>
<td><strong>Artifacts</strong></td>
<td>Objects complying with mandated specifications</td>
<td>Objects meeting conventions, standards</td>
<td>Objects possessing symbolic value</td>
</tr>
</tbody>
</table>

Table 2 – Firm Level Descriptive Statistics

<table>
<thead>
<tr>
<th></th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Median</th>
<th>Stand. Dev.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Firm Age (years)</td>
<td>2</td>
<td>175</td>
<td>36.2</td>
<td>23.0</td>
<td>37.4</td>
</tr>
<tr>
<td>Market Cap. **</td>
<td>12.7</td>
<td>63,788</td>
<td>7,544</td>
<td>1,961</td>
<td>13,055</td>
</tr>
<tr>
<td>Leverage</td>
<td>0.0%</td>
<td>105.2%</td>
<td>20.9%</td>
<td>17.6%</td>
<td>19.3%</td>
</tr>
<tr>
<td>Assets **</td>
<td>4.85</td>
<td>536,780</td>
<td>21,076</td>
<td>1,721</td>
<td>77,248</td>
</tr>
<tr>
<td>Sales **</td>
<td>0</td>
<td>34,194</td>
<td>4,224</td>
<td>1,053</td>
<td>6,883</td>
</tr>
<tr>
<td>Return on Assets</td>
<td>-28.3%</td>
<td>42.8%</td>
<td>6.0%</td>
<td>5.4%</td>
<td>9.6%</td>
</tr>
<tr>
<td>EPS</td>
<td>(3.32)</td>
<td>6.95</td>
<td>1.72</td>
<td>1.33</td>
<td>1.80</td>
</tr>
<tr>
<td>Board Size</td>
<td>3</td>
<td>17</td>
<td>9.53</td>
<td>9</td>
<td>3.0</td>
</tr>
<tr>
<td>CEO Tenure</td>
<td>1</td>
<td>40</td>
<td>7.25</td>
<td>5.0</td>
<td>7.3</td>
</tr>
<tr>
<td>% of Board independent</td>
<td>44%</td>
<td>100%</td>
<td>75%</td>
<td>78%</td>
<td>14%</td>
</tr>
</tbody>
</table>

** in $ millions

**Dummy Variables:**

- Cross-listed on US exchange: 37% of firms (n=105)
- Dominant Shareholder: 53% of firms (n=105)
- CEO/Chair Split: 87% of firms (n=105)
- Chair Independent: 61% of firms (n=105)
- Director Share Plan: 73% of firms (n=105)
The results for “To be Effective” are for the 2006/07 survey – a Wilcoxon signed rank test showed no significant difference between the 2004/05 and 2006/07 surveys on this question so only the 2006/07 results are shown.
Table 3 - Board-Management Ties; Board as Strategic Asset

Q.14 In your opinion, how does the CEO regard the board? (2006/2007 survey)

Q.4 In your experience, how do CEOs regard their boards? (2004/2005)

<table>
<thead>
<tr>
<th>Descriptive</th>
<th>Major obstacle to be tolerated</th>
<th>Minor hindrance</th>
<th>Neutral</th>
<th>Generally helpful</th>
<th>Strategic asset</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999/2000 (5 years ago)</td>
<td>1.9%</td>
<td>23.3%</td>
<td>36.0%</td>
<td>35.2%</td>
<td>3.6%</td>
</tr>
<tr>
<td>2004/2005 (now)</td>
<td>0.3%</td>
<td>3.6%</td>
<td>10.4%</td>
<td>65.1%</td>
<td>20.6%</td>
</tr>
<tr>
<td>2006/2007 (now)</td>
<td>1.0%</td>
<td>1.0%</td>
<td>3.8%</td>
<td>54.3%</td>
<td>40.0%</td>
</tr>
<tr>
<td>2004/05 (effective)</td>
<td>0.0%</td>
<td>0.0%</td>
<td>0.8%</td>
<td>23.0%</td>
<td>76.2%</td>
</tr>
<tr>
<td>2006/07 (effective)</td>
<td>0.0%</td>
<td>0.0%</td>
<td>0.0%</td>
<td>21.0%</td>
<td>79.0%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Results</th>
<th>2004/2005</th>
<th>2006/2007</th>
<th>04/05(effective)</th>
<th>06/07(effective)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004/05 (now)</td>
<td>N/A</td>
<td>Z=4.21***</td>
<td>Z=14.55***</td>
<td>Z=8.12***</td>
</tr>
<tr>
<td>2006/07 (now)</td>
<td>N/A</td>
<td>Z= 4.95**</td>
<td>Z= 6.27***</td>
<td></td>
</tr>
<tr>
<td>2004/05 (to be effective)</td>
<td></td>
<td>N/A</td>
<td>Z=0.96</td>
<td></td>
</tr>
</tbody>
</table>

Z statistic:  * P<0.05, ** P<0.01, *** P<0.001  Wilcoxon signed-rank tests
Table 4 – Board-Management Ties; Openness of Communication

Q.11 How would you describe the nature of communication (e.g., information flow) between your board and management? (2006/2007 survey)

Q.28 How would you describe the nature of communication (e.g., information flow) between the board and management? (2004/2005 survey)

<table>
<thead>
<tr>
<th></th>
<th>Very closed</th>
<th>Closed</th>
<th>Neutral</th>
<th>Open</th>
<th>Very Open</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999/2000 (5 years ago)</td>
<td>1.7%</td>
<td>12.4%</td>
<td>32.7%</td>
<td>44.8%</td>
<td>8.5%</td>
</tr>
<tr>
<td>2004/2005 (now)</td>
<td>0.0%</td>
<td>0.8%</td>
<td>5.2%</td>
<td>64.8%</td>
<td>28.6%</td>
</tr>
<tr>
<td>2006/2007 (now)</td>
<td>0.0%</td>
<td>1.9%</td>
<td>3.8%</td>
<td>56.2%</td>
<td>38.1%</td>
</tr>
<tr>
<td>2004/05 (to be effective)</td>
<td>0.0%</td>
<td>0.0%</td>
<td>1.1%</td>
<td>37.9%</td>
<td>61.0%</td>
</tr>
<tr>
<td>2006/07 (to be effective)</td>
<td>0.0%</td>
<td>0.0%</td>
<td>2.9%</td>
<td>34.3%</td>
<td>62.9%</td>
</tr>
</tbody>
</table>

Results

<table>
<thead>
<tr>
<th></th>
<th>2004/2005</th>
<th>2006/2007</th>
<th>04/05(effective)</th>
<th>06/07(effective)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004/2005 (now)</td>
<td>N/A</td>
<td>Z=1.68</td>
<td>Z=11.29***</td>
<td>Z=5.21***</td>
</tr>
<tr>
<td>2006/2007 (now)</td>
<td>N/A</td>
<td>Z=2.72**</td>
<td>Z=5.21***</td>
<td></td>
</tr>
<tr>
<td>2004/2005 (to be effective)</td>
<td>N/A</td>
<td></td>
<td></td>
<td>Z=1.12</td>
</tr>
</tbody>
</table>

Z statistic:  * P<0.05,   ** P<0.01   *** P<0.001  Wilcoxon signed-rank tests
Table 5 – Board-Management Ties; Nature of Interpersonal Interactions

Q.10 How would you describe the quality of interpersonal interaction between your board and management? (2006/2007 survey)

Q.27 How would you describe the quality of interpersonal interaction between the board and management? (2006/2007 survey)

<table>
<thead>
<tr>
<th>Descriptive</th>
<th>Very tense</th>
<th>Tense</th>
<th>Neutral</th>
<th>Collegial</th>
<th>Very Collegial</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999/2000 (5 years ago)</td>
<td>1.1%</td>
<td>6.8%</td>
<td>26.4%</td>
<td>55.7%</td>
<td>9.9%</td>
</tr>
<tr>
<td>2004/2005 (now)</td>
<td>0.0%</td>
<td>0.0%</td>
<td>0.0%</td>
<td>8.6%</td>
<td>66.7%</td>
</tr>
<tr>
<td>2006/2007 (now)</td>
<td>0.0%</td>
<td>1.0%</td>
<td>9.5%</td>
<td>69.5%</td>
<td>20.0%</td>
</tr>
<tr>
<td>2004/05 (to be effective)</td>
<td>0.0%</td>
<td>3.1%</td>
<td>17.2%</td>
<td>61.7%</td>
<td>18.1%</td>
</tr>
<tr>
<td>2006/07 (to be effective)</td>
<td>0.0%</td>
<td>0.0%</td>
<td>8.6%</td>
<td>66.7%</td>
<td>24.8%</td>
</tr>
</tbody>
</table>

Results

<table>
<thead>
<tr>
<th>Descriptive</th>
<th>2004/2005</th>
<th>2006/2007</th>
<th>04/05(effective)</th>
<th>06/07(effective)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999/2000 (5 years ago)</td>
<td>Z=4.52***</td>
<td>Z=4.76***</td>
<td>Z=5.54***</td>
<td>Z=5.65***</td>
</tr>
<tr>
<td>2004/2005 (now)</td>
<td>N/A</td>
<td>Z=2.27*</td>
<td>Z=2.37*</td>
<td>Z=2.40*</td>
</tr>
<tr>
<td>2006/2007 (now)</td>
<td>N/A</td>
<td>Z=1.22</td>
<td>Z=1.54</td>
<td></td>
</tr>
<tr>
<td>2004/2005 (to be effective)</td>
<td></td>
<td>N/A</td>
<td>Z=1.39</td>
<td></td>
</tr>
</tbody>
</table>

Z statistic: * P<0.05, ** P<0.01, *** P<0.001 Wilcoxon signed-rank tests
Table 6a: Board Involvement in Firm Affairs (Strategy)

Ordered Logistic Regression Models; dependent variable is reported level of collaboration. Model 1 is main effects; regression run for the independent variables without controls. Model 2 includes the controls. First number is the beta coefficient followed by the standard error. Data is from the 2006/2007 survey only.

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Model 1</th>
<th></th>
<th>Model 2</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Coef.</td>
<td>SE</td>
<td>Coef.</td>
<td>SE</td>
</tr>
<tr>
<td>Board involvement In Strategy</td>
<td>0.67</td>
<td>0.12***</td>
<td>0.71</td>
<td>0.13***</td>
</tr>
<tr>
<td>Controls</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management</td>
<td>0.18</td>
<td>0.23</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ROA</td>
<td>-0.00</td>
<td>0.01</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Leverage</td>
<td>-0.00</td>
<td>0.01</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm age</td>
<td>-0.00</td>
<td>0.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm size</td>
<td>0.14</td>
<td>0.21</td>
<td></td>
<td></td>
</tr>
<tr>
<td>CEO tenure</td>
<td>-0.09</td>
<td>0.04*</td>
<td>0.02</td>
<td>0.01*</td>
</tr>
<tr>
<td>Interaction Tenure</td>
<td>0.02</td>
<td>0.01*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chair Independent</td>
<td>-0.56</td>
<td>0.30†</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board size</td>
<td>0.01</td>
<td>0.05</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Blockholder</td>
<td>0.55</td>
<td>0.25*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>X-Listed</td>
<td>0.23</td>
<td>0.27</td>
<td></td>
<td></td>
</tr>
<tr>
<td>%BoardInd</td>
<td>2.32</td>
<td>1.07*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Director DSU</td>
<td>-0.45</td>
<td>0.29</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Year</td>
<td>0.27</td>
<td>0.26</td>
<td></td>
<td></td>
</tr>
<tr>
<td>LR chi²</td>
<td>31.0***</td>
<td></td>
<td>57.1***</td>
<td></td>
</tr>
</tbody>
</table>

† P<0.10    * P<0.05    ** P<0.01    *** P<0.001
Table 6b: Board Impact on the Performance of the Firm

Ordered Logistic Regression Models; dependent variable is reported level of collaboration. Model 1 is main effects; regression run for the independent variables without controls. Model 2 includes the controls. First number is the beta coefficient followed by the standard error. Data is from the 2006/2007 survey only.

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Model 1</th>
<th>Model 2</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Coef.</td>
<td>SE</td>
</tr>
<tr>
<td>Board Impact on Performance</td>
<td>0.58</td>
<td>0.13***</td>
</tr>
<tr>
<td></td>
<td>0.60</td>
<td>0.14***</td>
</tr>
<tr>
<td>Controls</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management</td>
<td>0.08</td>
<td>0.22</td>
</tr>
<tr>
<td>ROA</td>
<td>-0.01</td>
<td>0.01</td>
</tr>
<tr>
<td>Leverage</td>
<td>0.00</td>
<td>0.01</td>
</tr>
<tr>
<td>Firm age</td>
<td>-0.01</td>
<td>0.01</td>
</tr>
<tr>
<td>Firm size</td>
<td>0.15</td>
<td>0.25</td>
</tr>
<tr>
<td>CEO tenure</td>
<td>-0.09</td>
<td>0.04*</td>
</tr>
<tr>
<td>Interaction Tenure</td>
<td>0.02</td>
<td>0.01*</td>
</tr>
<tr>
<td>Chair Independent</td>
<td>-0.60</td>
<td>0.30*</td>
</tr>
<tr>
<td>Board size</td>
<td>0.01</td>
<td>0.05</td>
</tr>
<tr>
<td>Blockholder</td>
<td>0.48</td>
<td>0.24*</td>
</tr>
<tr>
<td>X-Listed</td>
<td>0.19</td>
<td>0.27</td>
</tr>
<tr>
<td>%BoardInd</td>
<td>2.30</td>
<td>1.05*</td>
</tr>
<tr>
<td>Director DSU</td>
<td>-0.29</td>
<td>0.28</td>
</tr>
<tr>
<td>Year</td>
<td>0.22</td>
<td>0.25</td>
</tr>
<tr>
<td>LR chi²</td>
<td>20.5***</td>
<td>45.5***</td>
</tr>
</tbody>
</table>

† P<0.10  * P<0.05  ** P<0.01  *** P<0.001
Table 6c: Board Knowledge of the Firm

Ordered Logistic Regression Models; dependent variable is reported level of collaboration. Model 1 is main effects; regression run for the independent variables without controls. Model 2 includes the controls. First number is the beta coefficient followed by the standard error. Data is from the 2006/2007 survey only.

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Model 1</th>
<th></th>
<th>Model 2</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Coef.</td>
<td>SE</td>
<td>Coef.</td>
<td>SE</td>
</tr>
<tr>
<td>Board knowledge</td>
<td>0.14</td>
<td>0.04***</td>
<td>0.15</td>
<td>0.05***</td>
</tr>
<tr>
<td>Controls</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management</td>
<td>0.09</td>
<td>0.23</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ROA</td>
<td>-0.00</td>
<td>0.01</td>
<td>-0.00</td>
<td>0.01</td>
</tr>
<tr>
<td>Leverage</td>
<td>-0.00</td>
<td>0.01</td>
<td>-0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Firm age</td>
<td>-0.00</td>
<td>0.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm size</td>
<td>0.21</td>
<td>0.21</td>
<td></td>
<td></td>
</tr>
<tr>
<td>CEO tenure</td>
<td>-0.11</td>
<td>0.04**</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interaction Tenure</td>
<td>0.02</td>
<td>0.01*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chair Independent</td>
<td>-0.58</td>
<td>0.29*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board size</td>
<td>-0.00</td>
<td>0.055</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Blockholder</td>
<td>0.55</td>
<td>0.25*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>X-Listed</td>
<td>0.25</td>
<td>0.26</td>
<td></td>
<td></td>
</tr>
<tr>
<td>%BoardInd</td>
<td>1.80</td>
<td>1.05†</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Director DSU</td>
<td>-0.27</td>
<td>0.28</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Year</td>
<td>0.28</td>
<td>0.25</td>
<td></td>
<td></td>
</tr>
<tr>
<td>LR chi²</td>
<td>11.4***</td>
<td></td>
<td>37.7***</td>
<td></td>
</tr>
</tbody>
</table>

† P<0.10     * P<0.05     ** P<0.01     *** P<0.001
Table 7: Collaboration (Actual versus Deemed Most Efficacious)

Ordered Logistic Regression Models; dependent variable is the difference between the reported actual collaboration and level of collaboration seen as most effective. Model 1 is main effects; regression run for the independent variables without controls. Model 2 is the full model that includes all controls. First number is the beta coefficient followed by the standard error. Data is from the 2006/2007 survey only.

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Model 1</th>
<th></th>
<th>Model 2</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Coeff.</td>
<td>SE</td>
<td>Coeff.</td>
<td>SE</td>
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<tr>
<td>Appropriate versus</td>
<td>0.91</td>
<td>0.16***</td>
<td>0.86</td>
<td>0.17***</td>
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<tr>
<td>actual board</td>
<td></td>
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<tr>
<td>involvement Strategy</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Controls</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management</td>
<td>-0.20</td>
<td>0.23</td>
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<tr>
<td>ROA</td>
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<td>0.02</td>
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<tr>
<td>Leverage</td>
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<td>0.01</td>
<td></td>
<td></td>
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<tr>
<td>Firm age</td>
<td>0.00</td>
<td>0.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm size</td>
<td>0.06</td>
<td>0.22</td>
<td></td>
<td></td>
</tr>
<tr>
<td>CEO tenure</td>
<td>0.05</td>
<td>0.04</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interaction Tenure</td>
<td>-0.01</td>
<td>0.01</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chair Independent</td>
<td>0.55</td>
<td>0.31†</td>
<td>0.31†</td>
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<tr>
<td>Board size</td>
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<td>0.05</td>
<td></td>
<td></td>
</tr>
<tr>
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<td>0.26*</td>
<td>-0.52</td>
<td>0.26*</td>
</tr>
<tr>
<td>X-Listed</td>
<td>-0.66</td>
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<td>-0.66</td>
<td>0.29*</td>
</tr>
<tr>
<td>%BoardInd</td>
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<td>1.09</td>
<td>-1.27</td>
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<tr>
<td>Director DSU</td>
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<td>0.30*</td>
<td>0.62</td>
<td>0.30*</td>
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<tr>
<td>Year</td>
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<td></td>
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<tr>
<td>LR chi²</td>
<td>34.3***</td>
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<td>63.5***</td>
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</table>

† P<0.10   * P<0.05   ** P<0.01   *** P<0.001
Table 8: Monitoring: Evaluation of Management on Strategy and Execution

Ordered Logistic Regression Models; dependent variable is monitoring evaluation score which is the sum of the scores on reported level of board involvement in evaluating management on strategy and on execution. Independent variables represent director reports on interpersonal interactions, communication and collaboration. Model 1 is main effects; regression run for the independent variables without controls. Model 2 is the full model that includes all controls. First number is the beta coefficient followed by the standard error. Data is from the 2006/2007 survey only.

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Model 1</th>
<th>Model 2</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Coeff.</td>
<td>SE</td>
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<tr>
<td>Interpersonal Interactions</td>
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<td>0.18</td>
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<tr>
<td>Communication</td>
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<tr>
<td>Collaboration</td>
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<td>0.14**</td>
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<td>Controls</td>
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<tr>
<td>Management</td>
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<tr>
<td>ROA</td>
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<tr>
<td>Leverage</td>
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<td>0.01</td>
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<td>Firm age</td>
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<td>CEO tenure</td>
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<td>0.04</td>
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<tr>
<td>Interaction Tenure</td>
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<td>0.01</td>
</tr>
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<td>Chair Independent</td>
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<td>0.26</td>
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<td>Board size</td>
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<td>0.05</td>
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<tr>
<td>Blockholder</td>
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<td>0.22**</td>
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<td>LR chi²</td>
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† P<0.10    * P<0.05    ** P<0.01    *** P<0.001
Table 9: Monitoring: CEO Compensation

Ordered Logistic Regression Models; dependent variable is aggregate compensation scores of the reported level of compensation appropriateness relative to key performance measures. Independent variables represent reports by directors on interpersonal interactions, communication and collaboration. Model 1 is main effects; regression run for the independent variables without controls. Model 2 is the full model that includes all controls. First number is the beta coefficient followed by the standard error. Data is from the 2006/2007 survey only.

<table>
<thead>
<tr>
<th>Independent Variables</th>
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<td>Coef.   SE</td>
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<tr>
<td>Interpersonal Interactions</td>
<td>0.20   0.19</td>
<td></td>
<td>0.18   0.20</td>
<td></td>
</tr>
<tr>
<td>Communication</td>
<td>0.56   0.17***</td>
<td></td>
<td>0.62   0.17***</td>
<td></td>
</tr>
<tr>
<td>Collaboration</td>
<td>0.05   0.14</td>
<td></td>
<td>0.16   0.14</td>
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<tr>
<td>Controls</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Management</td>
<td>-0.42   0.20*</td>
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<td>0.006  0.003†</td>
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<td>0.006  0.003†</td>
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<tr>
<td>Firm age</td>
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<td>0.006  0.003†</td>
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<tr>
<td>Firm size</td>
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<td>0.42   0.20*</td>
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<td>CEO tenure</td>
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<td>-0.03  0.04</td>
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<tr>
<td>Interaction Tenure</td>
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<td></td>
<td>0.01   0.01</td>
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<tr>
<td>Chair Independent</td>
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<td>0.93   0.27***</td>
<td></td>
</tr>
<tr>
<td>Board size</td>
<td>-0.00   0.05</td>
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<td>-0.00  0.05</td>
<td></td>
</tr>
<tr>
<td>Blockholder</td>
<td>-0.04   0.22</td>
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<td>-0.04  0.22</td>
<td></td>
</tr>
<tr>
<td>X-Listed</td>
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<td>0.37   0.24</td>
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<tr>
<td>%BoardInd</td>
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<td>-2.76  0.95**</td>
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<tr>
<td>Director DSU</td>
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<td></td>
<td>0.06   0.25</td>
<td></td>
</tr>
<tr>
<td>Year</td>
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<tr>
<td>LR chi²</td>
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<td>76.3***</td>
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† P<0.10   * P<0.05  ** P<0.01  *** P<0.001

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Table 10: Summary of Hypotheses and Results

<table>
<thead>
<tr>
<th>Hypothesis</th>
<th>Theoretical Argument</th>
<th>Prediction Test</th>
<th>Analysis Results</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>H1a</strong>: Director reports of board-management ties along the dimension of interpersonal interactions will be over time towards greater collegiality</td>
<td>Institutional Change Mimetic Processes</td>
<td>Wilcoxon signed-rank test for significance</td>
<td>Supported</td>
</tr>
<tr>
<td><strong>H1b</strong>: Director reports of board-management ties along the dimension of communication flow will be towards greater openness over time</td>
<td>Institutional Change Mimetic Processes</td>
<td>Wilcoxon signed-rank test for significance</td>
<td>Not supported Positive but not significant</td>
</tr>
<tr>
<td><strong>H1c</strong>: Director reports of board-management ties along the dimension of degree of collaboration will be towards greater collaboration over time</td>
<td>Institutional Change Mimetic Processes</td>
<td>Wilcoxon signed-rank test for significance</td>
<td>Supported</td>
</tr>
<tr>
<td><strong>H2a</strong>: Director reports on what is most effective regarding interpersonal interactions between the board and management will over time show support for greater collegiality</td>
<td>Institutional Change Cognitive Embeddedness</td>
<td>Wilcoxon signed-rank test for significance</td>
<td>Not supported Positive but not significant</td>
</tr>
<tr>
<td><strong>H2b</strong>: Director reports on what is most effective regarding openness in communication between the board and management will over time show support for greater openness in communication</td>
<td>Institutional Change Cognitive Embeddedness</td>
<td>Wilcoxon signed-rank test for significance</td>
<td>Supported</td>
</tr>
<tr>
<td><strong>H2c</strong>: Director reports on what is most effective regarding the degree of collaboration between the board and management will over time show support for greater collaboration</td>
<td>Institutional Change Cognitive Embeddedness</td>
<td>Wilcoxon signed-rank test for significance</td>
<td>Supported</td>
</tr>
<tr>
<td><strong>H3</strong>: The greater the reported degree of collaboration between the board and management, the more the board is involved in the firm’s strategy.</td>
<td>Institutional Change enactment versus symbolic Mimetic Processes</td>
<td>Ordered logistic regression Strategy coefficient positive Operations no significance</td>
<td>Supported</td>
</tr>
<tr>
<td><strong>H4</strong>: The greater the difference between reported degree of collaboration and what is deemed most effective, the greater the difference between reported actual board involvement in the affairs of the firm in strategy development and what level of involvement is deemed most effective.</td>
<td>Institutional Change enactment versus symbolic Mimetic Processes</td>
<td>Ordered logistic regression Strategy difference coefficient positive Operations no significance</td>
<td>Supported</td>
</tr>
<tr>
<td>Hypothesis</td>
<td>Theoretical Argument</td>
<td>Prediction Test</td>
<td>Analysis Results</td>
</tr>
<tr>
<td>---------------------------------------------------------------------------</td>
<td>--------------------------------------------------------------------------------------</td>
<td>------------------------------------------------------------------------</td>
<td>------------------</td>
</tr>
<tr>
<td><strong>H5</strong>: The greater the reported board’s impact on firm performance, the more collaborative the relationship between the board and management.</td>
<td>Institutional Change enactment versus symbolic Mimetic Processes</td>
<td>Ordered logistic regression Coefficient for impact is positive</td>
<td>Supported</td>
</tr>
<tr>
<td><strong>H6</strong>: The greater the board’s knowledge as reported by directors, the more collaborative the relationship between the board and management</td>
<td>Institutional Change enactment versus symbolic Mimetic Processes</td>
<td>Ordered logistic regression Coefficient for board knowledge is positive</td>
<td>Supported</td>
</tr>
<tr>
<td><strong>H7a</strong>: The greater the perception of more collegial interpersonal interactions between the board and management, the more engaged directors will be with management in performance of their monitoring duties with respect of evaluation of management</td>
<td>Agency Modified assumption; closer ties in shareholder interests</td>
<td>Ordered logistic regression Coefficient for interpersonal interaction is positive</td>
<td>Not supported</td>
</tr>
<tr>
<td><strong>H7b</strong>: The greater the reported openness in communication flow between the board and management, the more engaged directors will be with management in performance of their monitoring duties with respect of evaluation of management</td>
<td>Agency Modified assumption; closer ties in shareholder interests</td>
<td>Ordered logistic regression Coefficient for openness is positive</td>
<td>Supported</td>
</tr>
<tr>
<td><strong>H7c</strong>: The greater the reported degree of collaboration between board and management, the more engaged directors will be with management in the performance of their monitoring duties with respect of evaluation of management</td>
<td>Agency Modified assumption; closer ties in shareholder interests</td>
<td>Ordered logistic regression Coefficient for collaboration is positive</td>
<td>Supported</td>
</tr>
<tr>
<td><strong>H7d</strong>: The greater the reported collegiality of interpersonal interactions between the board and management, the more engaged directors will be with management in performance of their monitoring duties with respect to aligning CEO pay with performance</td>
<td>Agency Modified assumption; closer ties in shareholder interests</td>
<td>Ordered logistic regression Coefficient for interpersonal interaction is positive</td>
<td>Not supported</td>
</tr>
</tbody>
</table>

**Hypothesis** | **Theoretical Argument** | **Prediction Test** | **Analysis** |

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<table>
<thead>
<tr>
<th>Argument</th>
<th>Test</th>
<th>Results</th>
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</thead>
<tbody>
<tr>
<td><strong>H7e</strong>: The greater the reported openness in communication flow between the board and management, the more engaged directors will be with management in performance of their monitoring duties with respect to aligning CEO pay with performance</td>
<td>Agency Modified assumption; closer ties in shareholder interests</td>
<td>Ordered logistic regression Coefficient for openness is positive</td>
</tr>
<tr>
<td><strong>H7f</strong>: The greater the reported degree of collaboration between the board and management, the more engaged directors will be with management in performance of their monitoring duties with respect to aligning CEO pay with performance</td>
<td>Agency Modified assumption; closer ties in shareholder interests</td>
<td>Ordered logistic regression Coefficient for collaboration is positive</td>
</tr>
</tbody>
</table>
Appendix A

Board as Strategic Asset – NACD Blue Ribbon Report 2001

The National Association of Corporate Directors is the professional association for corporate directors in the United States and has been releasing annual Blue Ribbon Commission reports that address topics of interest to their membership. In 2001, the NACD released their Blue Ribbon Report on Board Evaluation: Improving Director Effectiveness. This report was notable as it advocated that the board of directors act as a strategic asset to the firm where the board, in addition to its monitoring role, provided coaching and advice to management on strategic issues faced by the firm. Some key attributes of the board as strategic asset are given below:

- Knows and understands the company’s business and competition
- Provides intelligent “capital”
- Performance-enhancing ideas
- Establish high, realistic standards of performance
- Enhance decision-making with rigorous analyses
- Energize management by empowering them and holding them accountable
- Attract and retain top leadership team
- Focus on strategic issues
- Link executive compensation to shareholder value

The list is a mix of both monitoring and service (collaboration) with knowledge and involvement in firm strategy explicitly mentioned. Prior research (Anderson, Melanson & Maly, 2007) found that directors and managers were able to generally discern the difference between a board acting as a strategic asset and being generally helpful.

This 2001 Blue Ribbon Commission has been a consistent top seller for NACD since its publication. In the wake of the 2003 NYSE listing requirement to disclose evaluation practices (endorsed by the SEC), the practice of board evaluation has steadily increased, according to NACD’s annual governance surveys. The use of board evaluation to refine performance and the Blue Ribbon Commission Report on Board Evaluation that encourages boards to become strategic assets through such a process both may be factors explaining the rise in boards reporting to be strategic partners to management, as found in this research.

Thank you for participating in this important governance research in Canada. This survey is voluntary and confidential. It will take 20 minutes to complete. Please fill in the demographic information below, as it critical to our research. We will not identify you.

DEMOGRAPHICS

PLEASE NOTE: This survey is company-specific. We ask that you respond based on your specific experience with company to which we addressed this survey. Only in this way can we understand the evolving relationship between a board and its management team.

Thus, when filling out this demographic section and the rest of the survey, please do so with this company specifically in mind.

1. Please indicate with a ☐ your role in respect of this company…
   - ☐ I am a DIRECTOR and/or ☐ I am an EXECUTIVE

   As a director, I serve as:
   - ☐ Board Chair
   - ☐ Committee Chair
   - ☐ Neither

2. Please indicate your gender:
   - ☐ I am male ☐ I am female

3. Please indicate your years of service with this company…

   As a director, I have served this company for:
   - ☐ less than 1 year
   - ☐ 1 year – 2 years
   - ☐ 2 year – 5 years
   - ☐ 5 year – 10 years
   - ☐ over 10 years

4. Please in years of service in general…

   I have been a director for:
   - ☐ less than 1 year
   - ☐ 1 year – 2 years
   - ☐ 2 year – 5 years
   - ☐ 5 year – 10 years
   - ☐ over 10 years

5. Please indicate your areas of expertise:

   - ☐ Finance/Accounting ☐ HR/Legal ☐ Information & Communication Technology
   - ☐ Marketing/Sales ☐ Operations ☐ Strategy
Governance Reform

1. How would you describe the impact of regulation on corporate governance effectiveness over the last 5 years?
   - None
   - Partial
   - Moderate
   - Large
   - Very Large

2. What has been the direction of that impact?
   - Very negative
   - Negative
   - Neutral
   - Positive
   - Very Positive

3. What has been the cumulative effect of the attention on governance over the last 5 years on board processes that:
   - None
   - Somewhat
   - Moderately
   - Largely
   - Very Largely
   a. Improve oversight of the business
   b. Enhance value of the business
   c. Limit downside risk
   d. Ensure compliance

4. Based on your board’s experience in the last 2 years, what degree of improvement you have seen in the…
   - None
   - Partial
   - Moderate
   - Large
   - Very Large
   a. Degree of director preparation
   b. Quality of board discussion
   c. Level of director assertiveness
   d. Level of management responsiveness
   e. Outcomes of board decisions

5. What impact does your board have on corporate performance?
   - None
   - Partial
   - Moderate
   - Large
   - Very Large

6. What impact do you have on your board?
   - None
   - Partial
   - Moderate
   - Large
   - Very Large

7. What are the main reasons your board engages in evaluation? If you do not conduct board evaluation, check here: 3.8

   Rank each reason from 1 – 5, in terms of importance to your board

   Most important ↔ Least important
   a. Compliance
   b. Board effectiveness
   c. Board – management relations
   d. Individual director development
   e. Director replacement

8. To what degree does the board evaluation process improve your board’s effectiveness?
   - None
   - Partial
   - Moderate
   - Large
   - Very Large

9. Please add any comments you may wish to add on governance reform:
Board and Management Relationships

10. How would you describe the quality of interpersonal interaction between your board and management?

Very tense  Tense  Neutral  Collegial  Very Collegial

a. Now
b. To be truly effective

11. How would you describe the nature of communication (e.g., information flow) between your board and management?

Very closed  Closed  Neutral  Open  Very Open

a. Now
b. To be truly effective

12. To what degree do directors communicate clearly and forthrightly about contentious issues when they:

None  Partial  Moderate  Large  Very Large

a. Disagree with the CEO/management
b. Disagree with another director
c. Lack necessary information
d. Pertain to CEO compensation

13. In making decisions, to what degree do directors choose to rely on the opinion of:

None  Partial  Moderate  Large  Very Large

a. the CEO
b. Management, other than the CEO
c. Other directors on their board
d. Investors
e. Analysts

14. In your opinion, how does the CEO regard the board?

Major obstacle  Minor  Neutral  Generally helpful  Strategic asset

to be tolerated  hindrance

a. Now
b. To be truly effective

Board Chair – CEO Relations

15. To what degree do you feel the Chair and CEO understand their respective roles?

None  Partial  Moderate  Large  Very Large

16. To what degree is there tension as a result of overlap in their roles?

Never  Rarely  Sometimes  Often  Very often

17. How has tension between the Chair and CEO, to the extent it exists, changed over time?

Getting much worse  Getting worse  About the same  Getting Better  Getting Much better

18. Please describe the nature and source of tension between the Chair and CEO and how it may best be resolved:
**Strategy and Operations**

Our research with directors, executives and investors indicates that their roles and responsibilities may be changing. Knowing how each sees their own role and that of others is important in understanding effective governance.

19. For each area of responsibility listed below, please indicate the **level of influence** among directors, executives and investors that you think:

   (a) currently exists (Actual Influence),  
   (b) should exist (Appropriate Influence)

   Please do so separately for their (I) involvement in and (II) evaluation of each of strategy, planning and execution. Note – influence can be shared or overlap.

<table>
<thead>
<tr>
<th></th>
<th>Actual Influence</th>
<th>Appropriate Influence</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>I – INVOLVEMENT</strong></td>
<td>Rate their actual and appropriate involvement in…</td>
<td>Rate their actual and appropriate evaluation of…</td>
</tr>
<tr>
<td></td>
<td>None 1 2 3 4 5</td>
<td>None 1 2 3 4 5</td>
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<td></td>
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<td>Moderate 1 2 3 4 5</td>
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<td>Large 1 2 3 4 5</td>
</tr>
<tr>
<td></td>
<td>Very Large 1 2 3 4 5</td>
<td>Very Large 1 2 3 4 5</td>
</tr>
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</table>

**Developing Strategy**
- Board of Directors
- Senior Management
- Institutional Investors
- Hedge Funds

**Creating Operational Plan**
- Board of Directors
- Senior Management
- Institutional Investors
- Hedge Funds

**Executing the Plan**
- Board of Directors
- Senior Management
- Institutional Investors
- Hedge Funds

**II – EVALUATION**
- Strategy / Direction
- Operational Plan
- Execution / Outcome
Risk Management
Our research indicates that directors, executives and investors are paying close attention to risk.

20. For each area of risk listed below, please indicate – for directors, executives and investors – how much each has of:
   (a) Risk knowledge (Actual level of Knowledge / Understanding) for evaluating risk management effectiveness
   (b) Risk accountability (Appropriate level of Responsibility / Accountability) for developing risk management systems to address each category of risk.
   Note – Responsibility/Accountability can be shared or overlap.

Please circle a rating (1 to 5) for each item below:

<table>
<thead>
<tr>
<th>Knowledge / Understanding</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Responsibility / Accountability</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
</tr>
</tbody>
</table>

**Financial Risk**

<table>
<thead>
<tr>
<th></th>
<th>Board of Directors</th>
<th>Senior Management</th>
<th>Institutional Investors</th>
<th>Hedge Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rate their actual knowledge and appropriate responsibility...</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
</tr>
</tbody>
</table>

**Operational Risk**

<table>
<thead>
<tr>
<th></th>
<th>Board of Directors</th>
<th>Senior Management</th>
<th>Institutional Investors</th>
<th>Hedge Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rate their actual knowledge and appropriate responsibility...</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
</tr>
</tbody>
</table>

**Regulatory and Compliance Risk**

<table>
<thead>
<tr>
<th></th>
<th>Board of Directors</th>
<th>Senior Management</th>
<th>Institutional Investors</th>
<th>Hedge Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rate their actual knowledge and appropriate responsibility...</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
</tr>
</tbody>
</table>

**Brand and Reputational Risk**

<table>
<thead>
<tr>
<th></th>
<th>Board of Directors</th>
<th>Senior Management</th>
<th>Institutional Investors</th>
<th>Hedge Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rate their actual knowledge and appropriate responsibility...</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
<td>1 2 3 4 5</td>
</tr>
</tbody>
</table>

21. To what degree does your board focus its attention on preventing downside risk?
   Not nearly enough  Not enough  Just enough  Too much  Far too much

Please provide below any comments you wish to add on risk:
Leadership

22. How much do you attribute overall company performance (good or bad) to your CEO's performance?

None Partial Moderate Large Very Large

23. How would you describe your CEO's absolute level of compensation today (excluding pension)?

Far too low Too low About right Too high Far too high

24. How would you describe the CEO's pension package?

Far too low Too low About right Too high Far too high

25. Which possible elements of CEO compensation best motivate CEO behaviour to best serve shareholder interests?

<table>
<thead>
<tr>
<th>Best able to motivate</th>
<th>Least able to motivate</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Cash</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>b. Unrestricted stock options</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>c. Restricted stock options</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>d. Unrestricted stock grants</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>e. Restricted stock grants</td>
<td>1 2 3 4 5</td>
</tr>
</tbody>
</table>

26. For each measure of performance listed below, please rate:
   (a) the degree to which CEO compensation should be tied to each metric
   (b) how well your CEO’s compensation actually reflected performance last year

Please circle a rating (1 to 5) for each item below:

1 2 3 4 5

<table>
<thead>
<tr>
<th>Degree to which CEO compensation should be tied to each metric</th>
<th>Degree to which CEO compensation actually reflected company performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Relative measures</td>
<td></td>
</tr>
<tr>
<td>Specific performance goals set by the Board for the company</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Specific performance goals set by the Board for the CEO</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Performance within the industry</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Performance against market index</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Economic measures</td>
<td></td>
</tr>
<tr>
<td>Growth in earnings per share</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Return on invested capital (ROIC)</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Growth in Market share</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Valuation (share price)</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Qualitative measures</td>
<td></td>
</tr>
<tr>
<td>Customer satisfaction</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Employee satisfaction</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Succession planning/development</td>
<td>1 2 3 4 5</td>
</tr>
<tr>
<td>Community Relations &amp; CSR</td>
<td>1 2 3 4 5</td>
</tr>
</tbody>
</table>

Notes:
1. "within industry" refers to your peers/competitors
2. "market index" refers to all companies on an exchange (for example; the S&P/TSX composite index)
3. "CSR" = Corporate Social Responsibility
27. For each area of responsibility listed below, please indicate for directors, the CEO and investors:
   (a) the **Appropriate level of Influence**
   (b) the **Appropriate level of Responsibility**

<table>
<thead>
<tr>
<th>Please circle a rating (1 to 5) for each item below</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Actual Level of Influence</th>
<th>Appropriate level of Responsibility</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>None</td>
<td>Some</td>
<td>Moderate</td>
<td>Large</td>
<td>Very Large</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Setting of CEO Compensation

|                                                | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 |
| Board of Directors                             |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| CEO                                            |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Institutional Investors                         |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Hedge Funds                                    |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |

### Evaluation of appropriateness of CEO compensation

|                                                | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 |
| Board of Directors                             |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| CEO                                            |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Institutional Investors                         |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Hedge Funds                                    |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |

Note: ¹Includes work done by the Compensation Committee for board deliberation.

### CEO Succession

28. For each area of responsibility listed below, please indicate for directors, the CEO and investors:
   (a) the **Appropriate level of Influence**
   (b) the **Appropriate level of Responsibility**

<table>
<thead>
<tr>
<th>Please circle a rating (1 to 5) for each item below</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Appropriate Level of Influence</th>
<th>Appropriate level of Responsibility</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>None</td>
<td>Some</td>
<td>Moderate</td>
<td>Large</td>
<td>Very Large</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Identification of CEO Successors

|                                                | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 |
| Board of Directors                             |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| CEO                                            |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Institutional Investors                         |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Hedge Funds                                    |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |

### Grooming of CEO Successors

|                                                | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 |
| Board of Directors                             |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| CEO                                            |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Institutional Investors                         |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Hedge Funds                                    |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |

### Selection of CEO Successor

|                                                | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 | 1 | 2 | 3 | 4 | 5 |
| Board of Directors                             |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| CEO                                            |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Institutional Investors                         |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
| Hedge Funds                                    |   |   |   |   |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |   | 1 | 2 | 3 | 4 | 5 |
29. In your opinion, what is the level of adequacy of CEO succession planning in your company today?

None          Partial        Moderate           Large       Very Large

30. Please add any comments you may have on CEO succession at your company:

31. Please add any comments you may have on compensation at your company:

In prior research, directors presented to us issues of concern. Below are four statements made by directors.

32. Please indicate the degree to which each issue is particularly relevant to your board today.

Please circle a rating (1 to 5) for each item below:

<table>
<thead>
<tr>
<th>Statement 1</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>“We are trying to find the right blend between fiduciary oversight and strategic support to management.”</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Statement 2</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>“Boards are expected to be more active today. We struggle to conduct oversight without seeming to interfere in the management of the business.”</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Statement 3</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>“The board’s role is to create long-term value. With regulation, we have become risk averse and spend a lot of time on compliance not performance.”</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Statement 4</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>“If strategy goes wrong, management must tell us how and why. But as the board, we will debate our own role in the failure and do some soul searching. It’s not easy to evaluate ourselves objectively.”</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
</tr>
</tbody>
</table>
APPENDIX C: 2004/05 CANADIAN DIRECTOR OPINION SURVEY

A – ROLE OF THE BOARD – Please answer based on your general experience as a director.

1. How would you describe the proper role of corporate directors in the business community (corporate life)?
   - Passive
   - Limited
   - Moderate
   - Active
   - Interventionist

2. Does the quality of corporate governance affect a company’s future performance?
   - No
   - Partially
   - Moderately
   - Largely
   - Completely

3. In your opinion, to what degree do directors “really know what’s going on” in the companies they govern?
   - None
   - Partial
   - Moderate
   - Large
   - Complete
   a. 5 years ago
   b. Now
   c. To be truly effective

4. In your experience, how do CEOs regard their boards?
   - Major obstacle to be tolerated
   - Minor hindrance
   - Neutral
   - Generally helpful
   - Strategic asset
   a. 5 years ago
   b. Now
   c. To be truly effective

5. What do you think is the effect of having separate Board Chair and CEO roles?
   - Very Negative
   - Generally Negative
   - No Effect
   - Generally Positive
   - Very Positive
   a. Overall
   b. On corporate governance
   c. On company performance
   d. On investor perceptions

6. Do you support or oppose the following?
   - Very Much Against
   - Somewhat Against
   - Not Sure
   - Somewhat Support
   - Very Much Support
   a. Overall
   b. On corporate governance
   c. On company performance
   d. On investor perceptions

* Director education is an external endeavour, attesting to an established level of knowledge in the field of corporate directorship.
** Professional directors are individuals who predominately earn their living by serving on boards of directors.
7. In your experience, to what degree does each of the following determine long term corporate performance?

<table>
<thead>
<tr>
<th></th>
<th>None</th>
<th>Partial</th>
<th>Moderate</th>
<th>Large</th>
<th>Complete</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Employees in general</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>b. CEO</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>c. Management (excluding CEO)</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>d. Board</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>e. Competitive and Market conditions</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>

8. Do you have any other thoughts on how the role of the board is changing or how it should change?

B – EVOLUTION IN GOVERNANCE – Please answer based on your general experience as a director.

9. To what extent have efforts intended to improve corporate governance succeeded?

<table>
<thead>
<tr>
<th></th>
<th>None</th>
<th>Partial</th>
<th>Moderate</th>
<th>Large</th>
<th>Complete</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Overall</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>b. Efforts from legislators / regulators</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>c. From investors</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>d. From directors</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>e. From managers</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>

10. What are the greatest impediments to improving board performance? Rank EACH option from greatest (1) to least (6):

- ☐ CEO resistance
- ☐ Insufficient director pressure
- ☐ Director resistance
- ☐ Insufficient regulatory pressure
- ☐ Lack of director independence
- ☐ Insufficient investor pressure

11. How much real change have you seen in the quality of board performance in the last two years?

<table>
<thead>
<tr>
<th></th>
<th>None</th>
<th>Partial</th>
<th>Moderate</th>
<th>Large</th>
<th>Complete</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Degree of director preparation</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>b. Quality of board discussion</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>c. Level of director assertiveness</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>d. Level of management responsiveness</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>e. Outcomes of board decisions</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>

12. In your view, how much additional pressure for changes in corporate governance would be helpful?

<table>
<thead>
<tr>
<th></th>
<th>None</th>
<th>Partial</th>
<th>Moderate</th>
<th>Large</th>
<th>Complete</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. In general</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>b. From legislators / regulators</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>c. From investors</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>d. From directors</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>e. From managers</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>
13. Who will drive changes in governance going forward? Rank EACH option highest (1) to lowest (5):

☐ Legislators / Top regulators  ☐ Top Directors  ☐ Directors  ☐ Investors  ☐ Media management

14. Does new governance regulation cause board attention to focus more on (Please check one):
   a. Preventing downside risk
   b. A balance of downside risk and upside potential
   c. Maximizing upside potential

15. What proportion of your time as a director is spent on board activities related to:
   a. Compliance issues
   b. Performance issues

16. How much additional time is required of you as a director because of corporate governance reform, as a percentage of the time spent on all board responsibilities?

17. To what degree have new requirements for more independent directors created more diversity on boards?
   ○ None  ○ Partial  ○ Moderate  ○ Large  ○ Complete

18. Has governance reform caused you to view directorship as more or less attractive?
   ○ Much less  ○ Less  ○ No impact  ○ More  ○ Much more

19. Has recent litigation against directors (e.g. Worldcom) caused you to view directorship as more or less attractive?
   ○ Much less  ○ Less  ○ No impact  ○ More  ○ Much more

20. To what degree is director non-independence a factor in corporate scandals?
   ○ None  ○ Partial  ○ Moderate  ○ Large  ○ Complete

21. Do you support or oppose the following?

a. More shareholder approvals
   Very Much Against  Somewhat Against  Not Sure  Somewhat Support  Very Much Support

b. Elect directors by slate
   ○  ○  ○  ○  ○

c. Elect directors individually
   ○  ○  ○  ○  ○

d. Ability to vote against individual directors on a slate
   ○  ○  ○  ○  ○
C – BOARD DYNAMICS – Please answer based on your experience as a director of the Canadian company with the highest market capitalization on whose Board you currently serve.

22. What is the market capitalization (CDS) of this company?
   ○ <100 million ○ 100 million – <1 billion ○ 1 billion – < 5 billion ○ 5 billion – 20 billion ○ > 20 billion

23. What impact does your board have on corporate performance?
   ○ None ○ Partial ○ Moderate ○ Large ○ Complete

24. What impact do you have on your board?
   ○ None ○ Partial ○ Moderate ○ Large ○ Complete

25. In your experience, how would you describe the level of board engagement?
   a. 5 years ago
   b. Now
   c. In the future

26. To what degree do directors share a common understanding and approach to their roles?
   ○ None ○ Partial ○ Moderate ○ Large ○ Complete

27. How would you describe the quality of interpersonal interaction between the board and management?
   a. 5 years ago
   b. Now
   c. To be truly effective

28. How would you describe the nature of communication (e.g., information flow) between the board and management?
   a. 5 years ago
   b. Now
   c. To be truly effective

29. To what degree do directors communicate clearly and forthrightly about contentious issues when:
   a. Directors disagree with the CEO
   b. Directors disagree with each other
   c. Directors lack necessary information
   d. The issues pertain to CEO pay

30. To what degree does the CEO control and shape what directors learn about the company?
   ○ None ○ Partial ○ Moderate ○ Large ○ Complete

31. To what degree do directors choose to rely on management presentation and opinion in making decisions?
   ○ None ○ Partial ○ Moderate ○ Large ○ Complete
32. What degree of trust do you currently see between CEOs and boards?

- **CEO’s trust of directors**
  - None
  - Partial
  - Moderate
  - Large
  - Complete

- **Directors’ trust of the CEO**
  - None
  - Partial
  - Moderate
  - Large
  - Complete

33. Do you support or oppose the following?

- **Director control over the agenda**
  - Very Much
  - Somewhat
  - Not Sure
  - Somewhat
  - Very Much

- **More time for open discussion**
  - Very Much
  - Somewhat
  - Not Sure
  - Somewhat
  - Very Much

34. Are there specific issues pertaining to board dynamics and board effectiveness that warrant further consideration?

D – **SENIOR EXECUTIVE COMPENSATION** – Please answer based on your general experience as a director.

35. How would you describe senior executive compensation today?

- Far too low
- Too low
- About right
- Too high
- Far too high

36. If executive compensation is too high, by what percentage?

- 20%
- 50%
- 100%
- 200%
- 500%

37. Is CEO compensation tied directly to company performance?

- 5 years ago
- Now
- To be truly effective

38. To which aspects of company performance should CEO compensation be tied?

- **Capital market performance**
  - Short term share price
  - Long term share price
  - Growth in market capitalization

- **Economic and competitive performance**
  - Growth in earnings
  - Growth in market share
  - Other (please specify)
39. To what extent should CEO compensation be tied to company performance relative to competitors?

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<tr>
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<th>Partial</th>
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<tr>
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</table>

40. CEO compensation should be approved by shareholders.

<table>
<thead>
<tr>
<th>Very Much</th>
<th>Somewhat</th>
<th>Not</th>
<th>Somewhat</th>
<th>Very Much</th>
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<tr>
<td>Against</td>
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In the following questions, the terms “unrestricted” and “restricted” refer to conditions placed on the exercise of stock options or grants. Under conditions of restriction, directors can place time or performance constraints in the form of vesting, holding and/or hurdle requirements. Unrestricted stock options or grants may be exercised at will by the recipient.

41. To what degree do these elements of executive compensation motivate behaviour in the interest of shareholders?

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<tr>
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<tr>
<td>b. Unrestricted stock options</td>
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<tr>
<td>c. Restricted stock options</td>
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<tr>
<td>d. Unrestricted stock grants</td>
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<tr>
<td>e. Restricted stock grants</td>
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<tr>
<td>f. Pension benefits</td>
<td>O</td>
<td></td>
<td>O</td>
<td>O</td>
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<tr>
<td>g. Executive perquisites</td>
<td>O</td>
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42. What’s the proper mix of executive compensation to align interests with shareholders? (Specify % – Sum to 100%)

<table>
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<tr>
<th>0%</th>
<th>20%</th>
<th>40%</th>
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<td>d. Unrestricted stock</td>
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<td>e. Restricted stock</td>
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43. To what degree does executive compensation plan design have the potential to induce unethical or illegal behaviour?

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E – BOARD COMPENSATION – Please answer based on your general experience as a director.

44. How would you describe board compensation today?
   ○ Far too low ○ Too low ○ About right ○ Too high ○ Far too high

45. a. If board compensation is too high, by what percentage?
   ○ 20% ○ 50% ○ 100% ○ 200% ○ 500%
b. If board compensation is too low, by what percentage?
   ○ 20% ○ 50% ○ 100% ○ 200% ○ 500%

46. To what extent should board compensation be tied to company performance relative to competitors?
   None ○ Partial ○ Moderate ○ Large ○ Complete

47. Board compensation should be approved by a non-binding vote of shareholders.
   Very Much Against Somewhat Against Not Sure Somewhat Support Very Much Support
   ○ ○ ○ ○ ○ ○

F – BOARD EVALUATION – Please answer based on your general experience as a director.

48. How many US boards on which you currently serve engage in formal performance evaluation for each of...
   a. Full Board ○ ○ ○ ○ ○ ○
   b. Board Chair ○ ○ ○ ○ ○ ○
   c. Committees ○ ○ ○ ○ ○ ○
   d. Committee Chairs ○ ○ ○ ○ ○ ○
   e. Individual directors ○ ○ ○ ○ ○ ○
   f. CEO ○ ○ ○ ○ ○ ○

49. If you serve on a board that does not do formal performance evaluation, would you recommend that it start?

Please check for which of the following you would recommend conducting formal evaluation:

☐ Full board ☐ Board Chair
☐ Committees ☐ Committee Chairs
☐ Individual directors ☐ CEO
☐ Other (please specify) _________________________

If you serve on a board that engages in formal board evaluation, please answer the following:

50. How often does the evaluation process take place? Every □ years.

51. What effect does the board evaluation process have on improving board performance?
   ○ None ○ Partial ○ Moderate ○ Large ○ Complete
52. What is the primary reason(s) your board engages in evaluation? (Please check all that apply)
☐ Compliance
☐ Director replacement
☐ Individual director development
☐ Board effectiveness
☐ Board – management relations
☐ Investor pressure

53. What method(s) is used to conduct evaluation? (Please check all that apply)
☐ Questionnaire for directors
☐ Questionnaire for senior managers
☐ Interviews with directors
☐ Interviews with senior managers

54. Who takes responsibility for the conducting the board evaluation process (Please check all that apply)
☐ Full board
☐ Governance committee / governance committee chair
☐ Board Chair
☐ CEO
☐ Lead / presiding director
☐ Board secretary / legal counsel

55. Who conducts the board evaluation process (i.e., collects, analyzes and feeds back data)? (Please check all that apply)
☐ Board Chair
☐ CEO
☐ Lead / Presiding director
☐ Board secretary / legal counsel
☐ Governance Committee Chair
☐ External consultant

56. Do you have any recommendations for making evaluation more palatable or effective?

DEMOGRAPHICS – Please complete this section, as it is critical to our understanding of your responses.

Your experience as a non-executive director:
1. In your lifetime, on how many TSE boards have you served?  
2. Currently, on how many TSE boards do you serve?  
3. Currently, on how many boards do you serve? U.S.  Canadian  Other  
4. In your lifetime, on how many Canadian publicly-traded boards have you served?  
5. What percentage of your professional time is spent, collectively, serving these boards?  
6. Cumulatively, how many years of board experience do you have as a non-executive director?  

Your experience as a CEO:
7. In your lifetime, for how many companies have you served as CEO?  
8. Currently, do you serve as CEO of a TSE company?  ○ Yes ○ No  
9. Cumulatively, how many years of board experience do you have as a CEO?  

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APPENDIX D – KEY VARIABLES AND DESCRIPTIVE STATISTICS

Note: For board-management tie variables and results for both 2004/05 and 2006/07 surveys, see tables 3, 4 and 5 above.

2006/2007 Canadian Director Survey (response rates are in percent)

Mimetic Test Variables:

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Q.19-I Involvement in; Developing Strategy - **Actual** influence – Board

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Q.19-I Involvement in; Developing Strategy – **Appropriate** influence – Board

<table>
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Q.19-I Involvement in; Executing Plan - **Actual** influence – Board

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Q.19-I Involvement in; Executing Plan – **Appropriate** influence – Board

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Q.20 Financial Risk – **Actual** Knowledge – Board

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Q.20 Operational Risk – **Actual** Knowledge – Board

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Q.20 Regulatory & Compliance Risk – **Actual** Knowledge – Board

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Q.20 Brand & Reputational Risk – **Actual** Knowledge – Board

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Monitoring Variables (Board Evaluation of Management):

Q.19-II Evaluation of; Strategy - **Actual** influence – Board

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Q.19-II Evaluation of; Strategy – **Appropriate** influence – Board

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Q.19-II Evaluation of; Execution - **Actual** influence – Board

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Q.19-II Evaluation of; Execution – **Appropriate** influence – Board

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Monitoring Variables (Alignment of Compensation with Firm Performance):

Q.26 CEO Compensation **actually** tied to; Performance goals set by Board for the CEO

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Q.26 CEO Compensation **actually** tied to; Growth in EPS [earnings per share]

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Q.26 CEO Compensation **actually** tied to; ROIC [return on invested capital]

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