BREAKING WITH THE PAST:

THE NEED FOR DISRUPTIVE INNOVATION IN THE GOVERNANCE OF SOCIAL ENTERPRISES

SUMMARY

In this report, KULAK explains the need for a hybrid governance structure in social enterprises to maintain the balance between the social and the economic

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Due to pressures of marketization and professionalization, social enterprises are recently experiencing a dynamic evolution from organizations with a purely social mission towards hybrid organizations. From a governance point of view, this evolution asks for a hybrid governance structure to maintain the balance between the social and the economic. In this paper, we provide further insights in the governance in social enterprises in several ways. First, we take a closer look at social enterprises with the aim to compare the types of board configurations used in these organizations with those typically used in profit-driven organizations. Second, we focus our attention on social enterprises that innovate their board composition by appointing board members with a non-social background in their board of directors. Building on behavioral theory, we provide a dynamic perspective on changes in board composition and evaluate to which extent decision making processes change accordingly. We suggest that a disruptive innovation of the board is necessary in order to arrive at a hybrid governance structure.

INTRODUCTION

Throughout the world, organizations in the social sector have a long tradition to solve societal problems such as poverty, environmental pollution and drug abuse (Dees, 1998; Smith, 2010). The historical context of the social sector prompts the assumption that social enterprises[1] have a purely social purpose (Mason et al., 2006). However, this picture has been changing gradually since the 1990s (Smith, 2010; Dees, 1998; Sanders, 2012). Stimulated by remarkable political and social changes which have made their environment more competitive and uncertain, social enterprises are increasingly forced to break their tradition by adopting methods and values of the market to guide their operations (Eikenburry & Kluver, 2004). As a result, social enterprises are undergoing a gradual change of marketization and commercialization that have pushed them toward more business-like organization (Weerawerdena et al., 2010). Thereby, the social sector comprises a progressively diverse set of organizations with hybrid structures including for-profit and nonprofit logics (Smith, 2010; Pache and Santos, 2012).

Literature has identified several of political and social changes which are crucial to this process of commercialization and hybridization of social enterprises. First of all, the structural reforms of the social sector carried out by the governments have a played a dramatic role in changing the environment of NPO (Cornforth, 2003a; Borzaga et al., 2014). Common changes included: government cutbacks for public services (Boschee, 1998; Dart, 2004; Eikenberry & Kluver, 2004; Borzaga et al., 2014), government outsourcing in favor to the private sector (Dees, 1998) and privatization of social services (Borzaga et al., 2014). Clearly, these reforms have led to greater uncertainty for social enterprises by introducing greater competition from the private

[1] In this paper, we consider non-profit social enterprises that need to adopt more business-like activities, processes, and structures. While beyond the scope of our paper, the conceptualization of hybrid governance applies also applies to newly founded social enterprises that pursue social as well as economic goals.

market. Particularly, the resulting uncertainty pushes social enterprises to find other ways of income generation to realize their social mission (Eikenberry & Kluver, 2004). Thereby, these organizations are adopting commercial alternatives to traditional sources of funding. This trend has been intensified by the financial crisis, as it has increased the competition for available funds (Smith, 2010).

While traditional social enterprises still occupy a prominent social focus, the expectations towards these organizations have changed quite significantly. Many advocate that market disciplines should exert more influence in the social sector and thus social enterprises should become more business-like (Maier et al., 2014). It is encouraged such that social enterprises can gradually become self-financing (Mason et al., 2006). By now, it is well recognized how the external environment offers a great deal in explaining the changing course of social enterprises to become more business-like. Driven by the demands of the environment, social enterprises are strategically deciding their new course and shaping their own organizational processes. This implies that the hybridization among social enterprises is a strategy to cope with the more complex environment. For instance, in search of legitimacy and accountability, managers feel internal pressure to adopt business-like goals and processes (Smith, 2010; Wellens & Jegers, 2014). In short, the hybridization of social enterprises reflects the public reforms, financial crisis, pro-business zeitgeist and the responses to these changes of individual organizations.

Following Dart (2004), the strategical transformation can be understood in terms of goals, service delivery models and management. Due to commercialization and professionalization pressures, social enterprises are increasingly expected to adopt market disciplines to guide their organizational practice, planning and behavior – i.e. marketization (Maier et al, 2014). Imprinting new organizational logics requires the services of skilled professionals and thus social enterprises are increasingly required to combine their traditional social expertise with commercial awareness (Smith, 2010; Eikenberry & Kluver, 2004). The need of this expertise generates an internal demand for professionalization to manage these new logics. As a result both the internal and external pressures echo in calls for professionalization of the social sector. Professionalization generally describes the conviction that experts should be in charge (Salamon, 1999).

By now, the professionalization in terms of management abilities and the adoption of formalized practices has already taken place (Ebrahim et al, 2014; Schiller, 2013). Paralleling these developments in how social enterprises are managed, the board of these organizations should be questioned. Boards as the ultimate decision-making body are considered to a play a crucial role in managing the hybridization of social enterprises and its resulting social-business tensions (Battilana & Doradao, 2010). Unfortunately, boards of social enterprises often lack the ability to deal with the risks and demands of both the increasingly commercial expectations of internal management and external environment (Conforth, 2014). Since a change in organizational strategy may be facilitated through a change in boards (Hillman et al., 2000), innovations in board governance are required. In order to be able to effectively pursue this hybrid strategy, board governance of social enterprises should transfer towards more hybrid governance models (Bruneel et al, 2016). Hybrid governance structures imply that the composition of the board reflects both the social and the economic. The combination of profit and nonprofit logics is central to the board innovations of social enterprises (Battilana & Lee, 2014). Hence hybridization requires not only the commitment of management, but also the professionalization of boards (Smith, 2010).

So-far, too little attention has been given to boards in social enterprises and how they are influenced by the commercialization and professionalization wave of the social sector (Cornforth, 2012). This is somewhat surprising, as boards serve as a connection between the organization and its external environment (Ebrahim et al., 2014). As firms respond to changes in their environment by altering board composition (Hillman et al., 2000), social enterprises have gradually changed the board composition in order to deal increasing pressure to commercialize and professionalize (Mason et al., 2006). Whereas boards in social enterprises had a prominent social and public component, these organizations are recruiting board members with business and entrepreneurial skills. In general, there is a consensus that the changing environment in which social enterprises operate promotes a more business-like focus which requires the presence of a broader set of skills at board level (Mason et al., 2006).

Nevertheless, just following the recommendations regarding board composition does not guarantee optimal board effectiveness (Finkelstein & Mooney; Forbes & Miliken, 1999; Van den Berghe & Levrau 2004). The classical governance theories such as agency theory and resource dependency theory make the assumption that firms can easily respond to changing environments by adjusting strategy, goals and governance. Nevertheless, there will be a time lag between the changing environment and the transition of the organizations. Changing an organization and its governance takes time. The transition phase between the optimal organizational model and the traditional model is often neglected. This requires more theoretical insight on how social enterprises can go through this transition phase effectively. In this paper, we seek to enhance our understanding of the hybridization of board composition in social enterprises through a dynamic lens building on behavioral theory. In what follows, we first provide an overview of the most common theories in governance research of for-profit corporate firms and link them with their associated ‘optimal’ board structures. After that, we will translate the conclusions drawn from the for-profit literature to the non-profit context. Next, we elaborate on the concept of hybrid governance and employ a behavioral perspective on board dynamics to introduce the need for disruptive innovation in the governance of social enterprises. We conclude with implications for research and practice. We provide brief extracts of interviews with CEOs and board members of social enterprises throughout the paper to illustrate our thinking.

THEORETICAL PERSPECTIVES ON BOARDS OF DIRECTORS

Our research question asks how social enterprises have to adapt their governance structure in their transition into hybrid governance structures. Most governance research, including this study, focuses on the board of directors as the locus of organizational governance (Low, 2006). Boards of directors play multiple roles in organizations, such as monitoring the CEO and the management team, providing advice and counsel to the CEO and providing the firm with legitimacy and access to various types of resources. A variety of theories have been proposed to try to understand the roles of boards, such as agency theory, stewardship theory, resource dependency theory and stakeholder theory (Cornforth, 2003). Each of these theories motivates their optimal board structure based on the specific role they appoint to the board of directors of an organization. Notwithstanding the fact that each of the theories was introduced in studies investigating the governance of for-profit business corporations, they can be usefully extended to shine a light on non-profit boards (Cornforth, 2003).

Agency Theory – the board for managerial control

In corporate governance literature, agency theory is most frequently applied to firms in which ownership and control are separated. Agency theory assumes that managers (i.e. agents) have goals and risk preferences that are not entirely aligned with the interests of the owners (i.e. principals). To reduce these agency problems to a minimum, decision control (i.e. ratification and monitoring of decision) should be separated from decision management (i.e. initiation and implementation of decisions) (Fama & Jensen, 1983). Agency theory therefore views the board as an instrument to safeguard principal's interests from possible opportunistic behavior of agents (Fama & Jensen, 1983; Shleifer & Vishny, 1997). From an agency point of view, the board of directors has a monitoring role, which consists of a set of related activities, such as the control of the firm's performance, the monitoring of firm's activities, and the assessment of CEO behavior (Johnson et al., 1996; Stiles & Taylor, 2001; Zahra & Pearce, 1989).

Thus, in order to maximize the board's ability to properly execute its monitoring role, board composition should be structured such that it reduces the influence of the CEO (and its management team) on the board of directors. Several measures can help achieve this objective. First, in order to allow the board to critically evaluate CEO and management performance, the roles of CEO and chairman of the board should be separated (i.e. no CEO duality). Second, a board consisting of a majority of non-executive board members, further reduces the influence of management on the board. Third, agency theory favors large boards over small boards because a large board requires more time and effort of the CEO to build consensus for a given course of action. In other words, when a board is large, the CEO's ability to influence is mitigated and it is more difficult for the CEO to dominate the board.

Stewardship Theory – the board for managerial empowerment

A second theoretical perspective on the role of boards comes from stewardship theory (Davis et al., 1997; Muth & Donaldson, 1998). In essence, stewardship theory challenges the idea of conflicting interests of owners and managers (cfr. agency theory) and assumes that managers will act as effective and loyal stewards of an organization's resources. Managers are driven by non-financial motives, including the need for recognition and achievement, the intrinsic satisfaction of successful performance, respect for authority and work ethic. Stewardship theory therefore views the board of directors as a partner of management rather than its monitor (Cornforth, 2003). The role of the board of directors is a strategic one: to work with management to improve strategy and add value to the decision-making process.

Thus, in order to maximize the board's ability to properly execute its stewardship role, board composition should be organized in a way that increases its ability to reach consensus on important decisions, which requires effective communication, coordination and optimal recognition and utilization of each director's skills and capabilities. Several measures can help achieve this objective. Firstly, a CEO also serving as chairman provides unified firm leadership builds trust and stimulates motivation to perform. Secondly, a board of directors dominated by executive directors provides a depth of knowledge, technical expertise, commitment to the firm and ease of communication needed for effective board functioning. Thirdly, small sized boards are preferred because it is typically associated with better communication, coordination and social cohesion, needed for strategic consensus building (Van den Berghe & Levrau, 2004).

Resource Dependency Theory – the board as boundary spanner

A third theoretical approach used in corporate governance research is the resource dependence theory. Resource dependence theory argues that the board of directors can play a crucial role in linking organizations with these external resource providers (Pfeffer & Salancik, 1978). Through their board, organizations can exert control over their environment by co-opting the resources needed to survive. The board of directors is therefore viewed as a mechanism to reduce environmental uncertainty and provide access to critical resources (Johnson, Daily & Ellstrand, 1996). In essence, the board is considered as (1) a provider of advice and counsel, (2) a channel of communication between the organization and the external environment, (3) a provider of preferential access to commitments or support coming from the external environment, and (4) a provider of external legitimacy.

With respect to the optimal board size, Pfeffer & Salancik state the following: "the greater the need for effective external linkage, the larger the board should be" (1978: 172). Board size should thus reflect the levels and types of resource dependencies facing the firm (Boyd, 1990; Hillman et al., 2000). A high number of linkages with external organizations and directors provide the firm's decision makers with more sources of information and a higher level of environmental awareness. Furthermore they also increase a director's, and consequently, the organization's prestige. Apart from a high number of external linkages, the board of directors should also provide the organization with a high diversity of external linkages. Firstly, linkages *among* directors of the organization provide communication opportunities and thus information exchange on the topics of concern. Secondly, linkages *between* directors of customers and their suppliers, for instance through interlocking directorates, allow firms to reduce the uncertainty about the availability of the required resources in the future and can perhaps even secure favorable treatment on both sides.

Stakeholder Theory – the board as stakeholder representative

A fourth theoretical perspective to look at boards of directors is stakeholder theory (Donaldson & Preston, 1995). The main distinction between stakeholder theory and the previously discussed theories lies in the way they look at the organization. Whereas the previous theories took a shareholder perspective of the organization, stakeholder theory assumes that corporate governance should be the arena for attending to the legitimate interests and well-being of all stakeholders, not only to those of equity shareholders alone.

One mechanism to do this is by giving board positions to different stakeholder representatives. By doing this, organizations will be more likely to respond to broader social interests than the narrow interests of one group (Cornforth, 2004). According to this view, the major role of the board of directors of an organization is to represent the interests of various constituencies and groups (Iecovich, 2005). Thus, implicit to this view, is the notion that individual expertise in governance is secondary to a claim to be a representative of a particular stakeholder group (Low, 2006). In contrast to the previous theories, where board members were chosen based on their ability to manage the assets of the organization, the stakeholder perspective selects board members based on who they represent.

Table 1: Summarizing Board Structure Recommendations

	Agency Theory	**Stewardship Theory**	**Resource Dependence Theory**	**Stakeholder Theory**
Board Size	large boards	small boards	large boards	large boards
Board Independence	outsiders	insiders	outsiders	outsiders
Board Diversity	no opinion	no opinion	high diversity	high diversity
CEO Duality	undesirable	desirable	no opinion	no opinion

We summarized the main conclusions regarding the board composition and structure of the four different perspectives in Table 1. First, with relation to board size, a large board is argued to be beneficial for monitoring, resource provision as well as stakeholder representation purposes.

However, too large a board may bring along negative side effects including communication and coordination problems and a risk of “social loafing”, which could hinder consensus building and monitoring activities (Forbes & Milliken, 1999; Van den Berghe & Levrau, 2004). Secondly, whether the CEO of the organization should also serve as chairman of the board or not depends on which role the organization ascribes to management: control (agency theory) or empowerment (stewardship theory). Thirdly, with relation to the insider/outsider ratio, we conclude that the board of directors should consist of a mix of inside, executive directors (stewardship theory), as well as outside, non-executive directors (agency theory, resource dependency theory, stakeholder theory). Fourthly, there is a need for board member diversity and complementarity. More diversity implies broader knowledge and expertise, access to a broader range of external resources and representation of a wider spectrum of stakeholders.

HYBRID GOVERNANCE: COMPOSITION AND STRUCTURE

Since most corporate governance research has been performed with for-profit organizations in mind, our overview of theoretical perspectives is also biased towards these organizations. In the next section, we will elaborate on how corporate governance in the non-profit sector is different from corporate governance in the for-profit sector.

Since non-profit organizations have no residual owners, the monitoring function of nonprofit boards has to be interpreted differently than that of for-profit boards, (Callen et al., 2010). However, the managers remain the ‘agents’ in the principal-agent reasoning. The principals, on the other hand, are not the owners or shareholders of the organization, but rather the representatives of the beneficiaries of the organization’s mission. In other words, the monitoring function of the board is not obsolete in the nonprofit context, since it remains valuable to monitor whether the organization engages only in those activities that are congruent with beneficiaries' expectations (Miller-Millesen, 2003). In the nonprofit sector, it is common to make a distinction between social performance and financial performance. Nonprofit organizations thus have to manage the potential tension between social and financial goals (Spear et al., 2009). As a result, the relationship between board performance and organizational performance may get quite complex, compared to for-profit organizations (Forbes & Milliken, 1999).

Nonprofit boards are considerably larger than for-profit boards and consist almost entirely of outsiders (Oster, 1995), representing different stakeholders. On the one hand, these multi-stakeholder boards have the potential benefit of bringing together the interests of different stakeholder groups. On the other hand, they have potential costs in the sense that these boards are potentially more conflictual and because reconciling the various interests of different stakeholders can bring large transaction costs. Therefore, an important role of the board of most non-profit organizations is to balance different stakeholder interests (Spear et al., 2009).

Boards in nonprofit organizations typically consist almost entirely of outsiders (O'Regan & Oster, 2005). Such board composition is to a large extent the result of the popular belief that inside directors are unlikely to monitor their CEO pushing to increase the number of outsiders in the board. However, it is becoming more difficult for non-profit organizations to recruit board members with the appropriate skills and experiences, especially those with financial, business and strategic skills (Spear et al., 2009).

Building on the insights from the different theoretical perspectives on governance and the literature on governance in nonprofit, we argue that the board composition of social enterprises should have a good balance of representatives of the social and the economic. This way, the board will have a variety of domain knowledge, diversity in expertise and problem-solving skills (Rindova, 1999). As a result, the board will be able to identify a broader set of issues and problems the organization is facing as well as developing a larger variety of potential solutions.

However, the boards of social enterprises should also include enough insiders. Recent research show that CEO-only board structures paradoxically enhances the CEOs' influence (Adams et al, 2005) and reduces monitoring efficiencies (Liu & Jirapon, 2008). Without other insiders in the board, the power of the CEO increases significantly through his information brokerage position: the CEO becomes the only source of information between the organization and the board (Joseph et al, 2014). This puts the CEO in a position where he can take advantage of the resulting information asymmetry within the board. This may lead to a "shocking gap" between what actually happened in the organization and what outside board members were told in the board meeting by the CEO (Roberts, 2002). Inside directors, such as for example the CFO, can form a countervailing power to the CEO be providing valuable firm-specific information and its competitive environment to the outside board members (Hillman et al, 2000). Agency theorists therefore advocate for including at least a number of inside directors next to the CEO whose primarily role is internal monitoring (e.g. Baysinger & Hoskisson, 1990). To avoid potential conflict between inside directors and the CEO, only the board should have the authority to fire top managers who serve as inside directors.

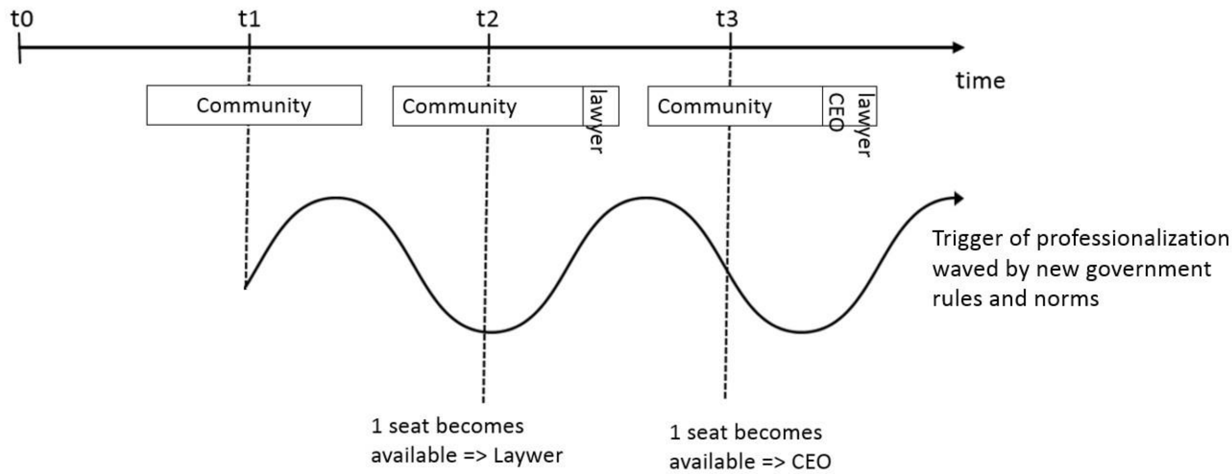
We also want to point to the specific role of the chairman in social enterprises. Whereas previous research emphasizes the importance of the leadership role and skills of the chair (e.g. Roberts, 2002; Leblanc, 2005), the role of the chairman in social enterprises is more challenging than in regular companies due to tension between the social and economic objectives and the representation of this tension in the board. The chairman plays a vital role in creating an environment which stimulates critical debate among directors: he/she has the ability to transform a board from a “minimalist board to a maximalist one” (Minichilli et al, 2009: 69). Such an environment is characterized by an open culture, critical debate and informal dialogue among board members (McNulty & Pettigrew, 1999). An important challenge of chairman is not to dominate the board meeting but to engage all directors in the discussions (Roberts, 2002); the chairman is no more equal than other directors (Levrau & Van Den Berghe, 2013. Depending on the background of the chairman, too much dominance of the chair could result in too much attention to the social at the expense of the economic (or vice versa) through prioritizing the social over the economic in the agenda for the board meetings and preventing the input of directors representing the economic(social). The chairman should act as supportive coach who tries to get the most out of the variety of expertise, skills, and social capital that social oriented and economic oriented directors bring to the board (Vanderwaerde et al, 2011); the chairperson’s leadership efficacy is an important determinant of board effectiveness (Leblanc, 2005; Gabrielsson et al, 2007; Machold et al, 2011). In essence, the social enterprise’s chairman should transcend the social-economic tension and be able to embrace the hybridity.

However, just following these recommendations regarding board structure and board characteristics does not guarantee optimal board effectiveness. (Finkelstein & Mooney, 2003; Forbes & Milliken, 1999; Van den Berghe & Levrau, 2004;). Boards of directors are episodic decision-making groups facing complex tasks, whose output is to a large extent cognitive in nature (Forbes & Milliken, 1999). This makes boards vulnerable to interaction difficulties, due to which their effectiveness largely depends upon social-psychological processes, such as group participation, critical discussion and exchange of information in the board (Forbes & Milliken, 1999; Milliken & Vollrath, 1991). Therefore, this study takes a step further than the classic structural approach and goes beyond the ‘usual suspects’ of board composition and structure. Instead, we will take a more contemporary behavioral approach (Pugliese et al., 2009; Van Ees et al., 2009) by focusing more on the bargaining politics and processes in boards.

THE EFFECTS OF MARKETIZATION AND PROFESSIONALIZATION ON BOARDS IN SOCIAL ENTERPRISES: A BEHAVIORAL PERSPECTIVE

Here we illustrate through an example how the board composition in social enterprises changes over time in response to the pressure of professionalization and marketization (see Figure 1). Before the shift in the external environment towards more professionalization and marketization, boards in social enterprises typically consist of managers of other non-profit organizations and representatives of local communities and local public policy. In response to the pressure emanating from the environment (time t_1 in Figure 1), social enterprises respond by changing the board composition. In line with resource dependency theory, organizations will use their board of directors as a mechanism to reduce environmental uncertainty and provide access to critical resources (Johnson et al, 1996). Business experts, who provide working knowledge on strategic decision making and internal firm operations of for-profit companies, and support specialist, who provide expertise in specific areas such as accounting and law, join the board. Importantly, these new board members can only join when a seat in the board becomes available (see t_2 and t_3 in Figure 1). Consequently, adjusting the board to the new external demands is a gradual process that can take several years.

FIGURE 1: Changing boards of social enterprises: a dynamic perspective



As illustrated in the figure above, boards in social enterprises incrementally adapt towards a more hybrid structure by offering board seats to outsiders not stemming from the social. However, although the composition of the board seems to reflect the trend of professionalization and marketization in social enterprises, this does not necessarily imply that also board processes enjoyed similar adjustments.

The governance literature suggests that history matters in corporate governance as there is a long-term persistence in board processes (Hermalin & Weisbach, 1998). The behavioral theory of the firm provides a useful lens to understand board processes and dynamics inside the board (van Ees et al., 2009). The behavioral theory of the firm is a key perspective to gain a better understanding of organizational behavior and decision-making (March & Simon, 1958; Cyert & March, 1963). A primary concept in this perspective is the concept of bounded rationality: decision makers in organizations are limited in their ability to gather and process information. Cognitive frames of decision-makers channel their attention towards information and stimuli which are in their comfort zone and also act as a filter for information processing (Tuggle et al, 2010). Decision-makers' cognitive frames are developed over time via education, job function, and sector in which they operate. An important characteristic influencing how the board functions is related to the homogeneity or heterogeneity among cognitive frames of board members (Murray, 1989).

Building on these insights, the homogeneity of cognitive frames of the board at time t0 is high as it consists only of decision-makers representing the social. The heterogeneity of cognitive frames increases when decision-makers from different working environments join the board at time t_2 and time t_3. Greater diversity on the board is a “double-edged sword for the functioning of the board (Forbes & Milliken, 1999). On the one hand, diversity increases the diversity of perspectives, information, and resources to the team. This, in turn, should stimulate cognitive conflict in the board. Cognitive conflict contributes to the quality of decision-making as more alternatives are considered and also considered much more carefully. On the other hand, diversity in boards makes communication and coordination among board members more difficult which may lead to affective conflicts in the group and difficult decision making (Cannella et al, 2008). Taken together, diversity in the board at time t_3 is higher than at time t_0 thus the dynamics in the boards would be very different between the two time periods due to significant differences in cognitive and affective conflict.

However, we argue that the board processes of social enterprises do not fundamentally change over time, despite bringing in board members with different backgrounds. Here, we draw on the concepts of the dominant coalition and routinization of decision-making to explain our thinking. The behavioral approach on governance pictures the board’s composition as a coalition of actors (Huse & Rindova, 2001). Organizational decision-making, goal setting and problem-solving is the result of a bargaining process between directors rather than the outcomes of a rational, objective thought process. Differences between boards on multiple attributes give rise to the formation of subgroups within the board. A useful concept to explain the emergence of subgroups is the faultline concept. Faultlines are hypothetical dividing lines that may split the group into subgroups based on the alignment of one or more demographic attributes (Lau & Murnigham, 1998). Thatcher and Patel (2012) point to self-categorization, social identification, and similarity attraction as theoretical mechanisms to explain the emergence of faultlines. Building on these mechanisms, people like to favour, trust, and cooperate with individuals that belong to the same social category and are similar to each other (Lau & Murningham, 2005; van Knippenberg et al, 2011).

Building on the concepts of coalitions and faultlines in groups, we argue that the dominant coalition in the board of social enterprises does not change fundamentally over time. At time t_0, the board consists of representatives of the social: managers of non-profit organizations and representatives of public policy. Arguably, there are no fundamental differences between these two groups in relation to attention allocation along the social-economic continuum in social enterprises. Both groups are primarily inclined to focus their attention towards the social of the organization. This group will work together for a relative long period before the first external member with a profile corresponding with the economic joins the board (time t_2 in Figure 1). During this time period, which spans several years, the group of representatives of the social will form the dominant coalition in the board and they will have developed a certain way of decision making and decision-making routines which are built up over time (Zahra & Filatochev, 2004). These routines are socially and historically constructed and direct the board's attention to certain elements of the identified problems (van Ees et al, 2009). The routinization process of decision-making is the outcome of a learning process between board members which results in procedures for information gathering, problem-solving, and decision-making. Importantly, these procedures become institutionalized over time (Zahra & Filatochev, 2004). As indicated in Figure 1, the dominant coalition and its associated process of decision-making haven't changed at time t_2 and time t_3. The above dynamic was described during an interview with a CEO of a social enterprise. The CEO, who had more than 15 years of experience in the for-profit sector, wanted to change the structure of the board:

> "They [existing board members] are very much removed from reality, especially the commercial aspects of our activities… I managed to get two new board members with industry experience appointed, but it is very difficult to realize real change. You cannot get rid of the existing ones! The historical directors serve already for 20 years in the board… they form the hard core in the board, which consists of 7 out of the 11 directors, who has all the power. I have the feeling that this is illustrative for the governance in the social profit sector". (Interview with CEO)

The presence of the dominant coalition also has an important impact on the decision-making processes of the board inside and outside board meetings. One director (BM_1) that was not part of the dominant coalition in the board of a social enterprise shared the following with us during an interview:

> "The other directors all have a mindset which is very much geared towards subsidies; I call it "subsidy thinking". When I joined, they asked me whether I could help finding sponsors for activities we organized. During one meeting I said "you are always looking for subsidies and sponsorships. Which initiatives could we take as an organization [to get money]? Approach it from a completely different perspective [by looking for alternative sources of income]". This was

> really a shock in the meeting! Also, I always have the impression that everything was already discussed outside the meeting by a small group of people who have all the power. Every year we went through the financial results. But there was very little room for discussion, there was no interpretation, no analysis, no action… decision were already arranged beforehand. Decisions which were not always in the best interest of the organization!"

ARRIVING AT HYBRID GOVERNANCE STRUCTURE: A NEED FOR DISRUPTIVE INNOVATION

Building on the behavioral perspective on corporate governance, boards that adopt gradually to the changing needs in the environment do primarily change in appearance but not in substance. The irregular replacement of representatives of the social by new board members representing the economic does not fundamentally change the processes in the board. Due to the presence of a dominant coalition representing the social and the routinization of the board's decision-making over time, these new board members will have little to no influence on the functioning of the board. Therefore, boards need to innovate disruptively in response to demand of the external environment for professionalization and marketization.

Breaking with the status quo: collective resignation of the board

Creating a good balance within the board between representatives of the social and the economic needs to go fast in order to avoid the negative influence of the social-focused dominant coalition. CEO_1 stressed the potential negative effects of this:

> "They do not understand the preparatory documents for the board meetings…They just do not realize that their skills are not enough." (Interview CEO_1)

In practice, all board members should resign collectively and a new board has to be installed. This need for collective resignation by board members was put forward by an honorary chairman of a large social enterprise. This social enterprise was confronted with a strong liberalization of the market which increased competition from abroad. This triggered a high need for professionalization, including the functioning of the board. This resulted in a number of very significant changes in the board: different structure (going from 9 to 7 directors, 3 external directors, and two deputy chairmen), profile description of directors and (deputy)chairman, formal selection procedure of directors by external recruitment agency, formal evaluation process of directors and (deputy)chairman, limitation of 12 years membership (3 x 4 years), and a maximum of eight years for the chairman (2 x 4 years). Very early on during the change process, the board members felt that they had to resign collectively:

> "We [the directors] all realized that we had to resign collectively. Is there another way if you really want to professionalize your board so drastically? The only other option was that all existing board members would serve their terms and that we would use the new procedures when a position became available. We would be busy for at least 5 years to make the transition! Resigning collectively also sends an important message to the management and employees: we are professionalizing as an organization and as a board, we are breaking with the past! Incremental, gradual change does not work because your signal is wrong! You need to show that the organization is moving towards a different structure, to a different functioning of the board." (Interview Honorary Chairman)

Importantly, such a disruptive innovation of the board also requires changing the chairman: The chairman of the board is the spokesman of the organization to its stakeholders. Replacing the chairman has an important signaling value to stakeholders:

> “When you do a major change and you set up a new governance structure but the chairman stays, then your stakeholders will ask: “what is changed?” So presenting a new chairman to our stakeholders was an important signal of the change process. (Interview with chairman of a social enterprise)

The table below gives an overview of the key characteristics of disruptive innovation in the board of social enterprises:

Table 1: key characteristics of disruptive innovation in the board of social enterprises

Characteristic	Motivation
Create balance between representatives of social and economic logic	to avoid overemphasizing one logic at the expense of the other
Create balance fast, not gradually	to avoid negative influence of a dominant coalition
Change the chairman	to give an important signal of the change process to stakeholders
Reduce the total board size	to avoid difficult and less efficient decision making
Include inside board members, not only outsiders	to avoid inside information monopoly of CEO

Making disruptive board innovation possible: the role of the bylaws

A crucial prerequisite of board innovation in social enterprises is to change the bylaws of the organization in a number of ways. First, social enterprises need to set term limits to board membership. In contrast to for profit companies where directors can typically serve only two terms of four or six years, reappointment of board members in social enterprises is unlimited.

Board members in social enterprises typically have long tenures; periods of 15 years or longer are no exception.

> “A lot of the directors have a seat in our board for 15 years and they want to keep that seat. It is very difficult and delicate to say to those directors: “you are been here now for 15 years and, to be honest, we already have too many directors with your type of expertise so… A limited term for board members: this is not done in our sector!” (Interview CEO_2)

A potential threat is that board members with long tenure may become too close with management and therefore feel less inclined to question management critically (Finkelstein & Mooney, 2003). In addition, the organization may face new strategic challenges for which the board members with long tenure do not have the rights expertise. Consequently, setting a term limit of board membership in the bylaws is necessary to keep the board fresh (Finkelstein & Mooney, 2003). Another important benefit of using limited terms is that there is less chance of the formation of a dominant coalition and concentration of power in the board. As stated by the Honorary Chairman of the board of the organization that underwent a disruptive innovation in the board:

> “Directors can serve three terms of four years, thus maximum of 12 years). The new bylaws also include an extra condition for the chairman: maximum eight years. The time that people stay longer in the board, and especially the chairman, is over. They build too much power over time. For example, I served 18 years as chairman, I built up a lot of power, honestly, I had too much power. At a certain

> point in time, I had the feeling that I could do too much without having to give accountability."

Second, the boards of social enterprises are typically too large in order to be effective and efficient. The BM_1 shared with us the following:

> "There are way too many directors in our board! At least 15 people. More than half of those people are just sitting there, listening, and waiting until we all go to the diner. There are only two, three people who are really contributing to the discussion and challenging the chairman, the others are just nodding… Boards should only have seven to eight directors, each with their own expertise with some overlap so you can have good, fruitful discussions.

The organization that disruptively innovated its governance structure also reduced the number of directors from 13 to nine: "13 [directors] worked, but nine directors also works, and works more efficiently" (Interview with honorary chairman).

Third, the bylaws should also state a limit to the number of other board seats directors can take on. An important perquisite for board members to be able to perform their monitoring and services roles is that they have time to serve (Finkelstein & Mooney, 2003). Without adequate time, board members will be unlikely to go through the preparatory documents prior to the board meetings in sufficient detail. As a result, they will not be able to participate in the discussion during the meeting and contribute to the strategic decision-making process or even attend board meeting (Adams & Ferreira, 2008). In social enterprises, however, directors with a total number of five to ten board seats are not an exception.

Fourth, social enterprises should pay careful attention to the selection of outside board members and include a formal selection procedure in the bylaws. Board members should be chosen based on their professional qualifications: 1) the specific areas of expertise that are useful to the organization, 2) the representation of the organization's different stakeholders, and 3) the social capital they bring to the organization (Iecovich, 2005). However, whereas top management is recruited through a professional process, the search for new outside board members is too often limited to own networks (Van den Berghe & Levrau, 2004). The selection process is informal as "board members propose their colleagues", which implies that the existing board's composition is preserved and only changes on paper (Iecovich, 2005). Such boards do not work as there is little interaction and discussion between board members due to lack of cognitive diversity (Van den Berghe & Levrau, 2004). Special attention should go to the selection of the Chairman of the board as board leadership is critical to board effectiveness. As emphasized by Leblanc (2005: 655), "the choice of the chair of the board… could be considered to be the most important decision that a board of directors makes, other than selecting the CEO". In addition to the three selection criteria stated earlier, chairs should also be selected based on their leadership skills and ability to embrace the hybrid nature of social enterprises.

Fifth, the professionalization of the board in social enterprises also requires attention for the remuneration of directors. Similarly to most other non-profit organizations (Wellens & Jegers, 2014), social enterprises do not pay their board members as they are assumed to have altruistic motives to serve on the board. However, social enterprises require board members with different, complementary skills to the typical more social-oriented directors. Such directors include business experts who are active or retired executives in for-profit organizations and support specialists who provide expertise and networks in specific fields of expertise such as for example capital markets and law (Hillman et al, 2000). These people, however, may not necessarily have altruistic motives to join the boards of social enterprises. A chairman of a social enterprise pointed out to the challenge of complementing his board with more economic-oriented board members and the need for remuneration:

> “if you want to build a professional organization and you want to attract high quality people as directors, then you are subjected to the law of the market. These people are wanted and have opportunities to serve in the board of other organizations, so you have to pay them a competitive fee. Simple as that! (Interview with the chairman of a social enterprise).

Sixth, the bylaws should include a section outlining the evaluation of board members, especially at re-election. While evaluation is advocated to be of primary importance for good governance, there is still a very long way to go in the overwhelming majority of organizations (Van den Berghe & Levrau, 2004). In order not to jeopardize the cohesiveness in the board, such evaluation should be managed by an outside organization. By performing regular, formal evaluations, the contribution of each director to the board’s value-creation for the organization can be assessed transparently and will provide data that can be acted upon (Leblanc, 2005). The table below summarizes the key elements of the bylaws to facilitate disruptive innovation in boards of social enterprises.

Recommendation	Motivation
Set limits to board tenure	to avoid long tenured board members to become too close with management (which decreases monitoring) and with each other (which may lead to the formation of a dominant coalition). Long tenures may also lead to a large concentration of individual power of long tenured board members.

Set limits to # of board seats	to avoid attendance problems and limited time to prepare and contribute
Include formal selection procedure for outside board members	to avoid 'clones' of incumbent board members and lack of cognitive diversity
Assess hybridity of board chair candidates	to ensure his/her capacity to take on an active role as coach and team leader
Remunerate directors, pay a competitive fee	because remuneration increases attendance, efforts and feeling of responsibility of directors and because good directors are wanted and have many opportunities, also outside of the non-profit sector
Develop job descriptions outlining the duties, responsibilities and roles of individual board members.	to allow for regular, formal and transparent assessment of each director's contribution to value-creation

DISCUSSION

In this paper, we address how social enterprises can adjust their board composition and structure effectively in their transition into hybrid governance structure to deal with increasing pressure to commercialize and professionalize. We go beyond the classic structural approach by taking a dynamic approach which acknowledges the importance of historical and social constructed governance processes. Employing a behavioral perspective, our study develops and conceptualizes the need for disruptive innovation of the on board composition and structure of social enterprises. The professionalization of board composition is a gradual process since new board members can only join when seats in the board are available. As a result, the current board composition is a mirror of the history, implying that the traditional social orientation will still influence current board decision-makings. Hence the presence of this social orientation may hinder the transition towards effective hybrid board governance that encompasses both the social and the economic (Bruneel et al, 2016). Since the effectiveness of organizational adaptation hinges on the dominant board coalition (Brown & Iverson, 2004), only prominent shifts in power might influence the organization decision-making (Van Ees et al., 2009).

Implications for Research

Our analysis holds a number of implications for research. First, this paper suggests an important tension between the appearance of good governance versus substance of good governance in social enterprises (McNulty et al, 2011). Building on behavioral theory, we argue that the formation of dominant coalitions over time prevents boards in social enterprises to change board processes and decision-making even though board structure changes. Social enterprises professionalize the board by appointing members with a non-social background primarily for compliance reasons. These changes occur irregularly which implies that boards adapt slowly to the changing environment and that board processes do not change fundamentally. These new board members have little to no influence on the decision-making process due to the social-oriented dominant coalition. Our study, therefore, suggests that there is a need to go beyond composition and structure in studying governance (cfr. agency and resource-dependency), especially in the context of change and adaptation. Much more attention should go to the influence of past coalition formation, behavior, and decision-making on the current decision-making of boards (Spender, 1989).

Second, our research contributes to the studies on the concept of "hybridity". Battilana and Lee (2014) refer to hybridity as the state of being composed through the mixture of disparate parts. Existing research has studied hybridity primarily at the level of the organization: the combination of multiple organizational identities, the combination of multiple organizational forms and, the combination of multiple institutional logics (see Battilana & Lee, 2014 for a review). Bruneel et al (2016) argued that social enterprises should have a hybrid governance structure that include representatives of both the social and economic logic in order to avoid that attention focused on the overrepresented logic (Costanzo et al, 2014). Our study extends this research by arguing that hybridity in social enterprises is also needed at the individual level. More specifically, the chairman of the board should have experience with the social and the economic. As such, hybridity is a multi-level concept.

Third, our study contributes to institutional theory and decoupling. Decoupling is a process through which organizations in competing institutional environments often deploy formal, visual structures that meet institutional demands but does not result in changing business practices. These "ceremonial" activities are decoupled from the core of the organization and provide merely symbolic compliance (Westphal & Zajac, 1998). Decoupling allows organizations to achieve conformity to competing logics at the surface without having to develop and invest in the necessary structures and processes internally. We add to this literature by suggesting that decoupling also may occur at the board level. People with business experience are decoupled from the social-oriented, dominant coalition in the board as they are attracted for compliance rather than for their contribution to discussion and decision-making.

Implications for Practice

Our results are also valuable for practitioners. Our findings suggest that social enterprises need to recognize the importance of professionalizing both loci of organizational decision making: (i) the top management team (operational decision making apex) and (ii) the board of directors (strategic decision making apex). To date, social enterprises tend to underemphasize the board of directors in their professionalization efforts, in contrast to the rapidly evolving procedures and formalizations being introduced for top management teams. For instance, whereas the introduction of selection and evaluation procedures for members of the top management team becomes widely accepted, new board members are in many cases still proposed directly from the personal networks of existing board members. In other words, the selection of new board members is only rarely formalized and evaluation procedures are virtually nonexistent. We contend that it is important to highlight this remarkable trend that, with relation to the two loci of organizational decision making, professionalization is clearly occurring at different speeds. This can potentially lead to tensions within the social enterprise as these different speeds of professionalization could result in increasing alienation of operational and strategic decision-making. Therefore, in order to avoid unnecessary imbalances and tensions in the decision making team, social enterprises should keep in mind to professionalize their board of directors at the same pace of their top management team.

Future Research Areas

It is clear that our understanding of the concept of hybrid governance is evolving and becoming more defined as more scholarship appears on the subject. We have tried to show the importance of hybrid governance and the need for disruptive innovation of boards of directors to arrive at hybrid governance. However, much work remains to be done as we continue to unravel the role of governance in the context of hybrid organizations.

First, organizational professionalization does not happen overnight (Dekker et al., 2015). It is a gradual process with temporal dynamics (Howorth et al., 2016). However, few studies have explored professionalization as a process, but are cross-sectional analyses limited to analyzing the coexistence of specific variables (Howorth et al., 2016). Therefore, to get a dynamic perspective on the professionalization process, we encourage future scholarship in this area to make use of longitudinal research designs. This could, for instance, allow identifying how and when structural board adjustments are being reflected in organizational actions over time.

Second, we have emphasized the importance of the role of the chairman, specifically in social enterprises. It could be argued that in order to achieve hybridity at the board level, there is a need for hybridity at the individual chairman level. Future research could therefore develop measures for individual hybridity and, subsequently, empirically investigate how chairman hybridity impacts board processes, board leadership style, social-economic tensions at the organizational level, etc.

Third, it could also be interesting to examine to which extent it matters for the actual process of board change where the trigger for the governance innovation comes from. For instance, the trigger can come from external actors (e.g. the government) as well as from internal actors (e.g. the top management team or the board itself). The type of actor instigating the governance change impacts the type and form of sensemaking and sensegiving activities taking place (Gioia & Chittipeddi, 1991). Therefore, future research should examine whether and how the sensemaking and sensegiving activities of various change instigators impacts board change processes.

Fourth, our study shows that an adaptation or at least a careful examination of the bylaws of an organization is a prerequisite for board innovation. However, and to our surprise, very little, to no attention, is given to the bylaws in the governance literature. Future researchers are encouraged to examine the role of bylaws as a facilitator of organizational change in greater detail.

Fifth, whereas our study focused on nonprofit organizations experiencing pressure to focus more on economic objectives on top of their historically dominant social objectives, the reverse situation is also occurring increasingly. Today, some for-profit organizations are asked to address an ever stronger set of societal expectations (Santos et al., 2015), facing unprecedented demands related to their social and environmental sustainability next to their historically dominant economic objectives (Santos et al., 2015; Lee & Jay, 2015). Equivalently to the nonprofit organizations in our study, these for-profit organizations will have to find a way to achieve this imposed hybridity. Future research should consider this situation and examine how these organizations work towards hybridity and to which extent and how governance innovation plays a role in this context.

Finally, while beyond the scope of this article, future research could also examine the relationship between the board and the General Assembly. In essence, the General Assembly is the highest governing body and the board of directors has to give accountability to the General Assembly. Since for change to occur at the organizational level, existing value and meaning systems of the 'change instigator' have to be in line with the intended change (Gioia, 1986), hybridity should also be realized at the level of the General Assembly. Future research could examine the relationship between Board and General Assembly in the context of hybrid organizations.

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