Separation of Chairman and CEO Roles

• In theory, having a separate (independent) chair improves the ability of the board of directors to oversee management.

• Potential benefits:

  (+) Clearly distinguishes the roles of the board and management.

  (+) Eliminates conflicts in the areas of performance evaluation, executive compensation, succession planning, and the recruitment of new directors.

  (+) Gives one director clear authority to speak on behalf of the board.

  (+) CEO can focus completely on strategy, operations, and organizational issues.
KEY CONCEPTS

• However, separation of the chairman and CEO roles is not unambiguously positive.

• Potential disadvantages:
  
  (-) Artificial separation, particularly when effective chairman/CEO is already in place.
  
  (-) Duplicates leadership: less efficient decision making, internal confusion.
  
  (-) Recruitment of new CEO is more difficult if candidates expect to hold both titles.

Most research finds no evidence that independence status impacts corporate outcomes on average.

- Include only companies with stable chairman status over entire period.

Compare risk-adjusted stock price performance of companies with dual chairman/CEO to those that separate the roles.

Find no statistically significant difference in stock price returns.

Conclusion: independence status does not impact performance.
Dalton, Daily, Ellstrand, and Johnson (1998) perform a meta-analysis across multiple studies that examine the relationship between board leadership structure and firm performance.


Find no overall correlation between chairman status and performance.

Conclusion: independence status does not impact performance.

“It can be concluded, therefore, that there is no relationship between board leadership structure and firm performance.”
INDEPENDENCE DOES NOT IMPACT PERFORMANCE

- Balinga, Moyer, and Rau (1996) examine the impact of a change in independence status on performance.


- Findings:
  - Companies that separate (combine) the roles do not exhibit abnormal positive (negative) stock price returns around the announcement date.
  - No impact on future operating returns (ROA, ROE, and operating cash flow).
  - Weak evidence that an independent chair improves market-to-book values.

Conclusion: changes in independence status do not impact performance.

“Duality, although it may increase the potential for managerial abuse, does not appear to lead to tangible manifestations of that abuse.”
FORCED SEPARATION HARMS SHAREHOLDERS

- Dey, Engel, and Liu (2011) examine the impact of a forced separation of the chairman and CEO roles, due to shareholder pressure.


- Find that companies undergoing forced separation:
  - Exhibit significant negative returns around the announcement date.
  - Exhibit lower future operating performance (ROA) over 1- and 2-year periods.

Conclusion: forced separation is harmful to shareholders.

“Our evidence suggests that recent calls… for all firms to separate the roles of the CEO and board chair warrant more careful consideration, particularly considering firm-specific costs and benefits.”
Brickley, Coles, and Jarrell (1997) examine the motivation behind a decision to separate the chairman and CEO roles.

Sample: 661 companies (535 combined roles, 93 separate), 1988.

Findings:
- 82% that separate roles have former CEO, founder, or other officer as chair.
- CEOs who are not chair have lower tenure (2.9 years) than those who are (6.9 years).
- CEOs who are not chair become chair within five years, or leave the company.
- CEOs who become chair exhibit better performance (adjusted stock returns and ROC) than those who instead leave.

Conclusion: companies separate roles during succession and offer combined chairman/CEO role as incentive to perform.
Grinstein and Valles Arellano (2008) also examine the motivation behind a decision to separate the chairman and CEO roles.


Findings:

- Most firms separate roles to facilitate succession (consistent with Brickley et al.).
- A minority (20%) replace dual chair/CEO with fully independent chair.
- Companies are more likely to appoint an independent chair following poor performance (based on stock returns).
- Among these companies, performance improves the following year.

Conclusion: independent chair can improve performance in poorly performing companies.
Krause and Semadeni (2013) evaluate the impact of separation under different scenarios.

Sample: 1,053 companies, 2002-2006.

Findings (controlling for mean-reverting tendencies):

- Separation has positive effect following weak performance.
- Separate has negative effect following strong performance.
- Results are strongest when sitting CEO/chair is stripped of chairman title.

Conclusion: the impact of separation depends on the setting.

“The relevant question is not whether the roles should be separated, but rather when and how a firm should choose to separate them.”
CEO DUALITY IN PRIVATE COMPANIES

- Deman, Jorissen, and Laveren (2018) study the impact of CEO duality among privately held companies.

- Sample: 384 private Belgian companies, 2011.

- Findings:
  - No impact on financial performance, operating performance, strategy oversight.
  - No impact on advice or networking quality.
  - Negatively associated with CEO oversight, only if company has no controlling shareholder.

Conclusion: ownership structure might impact duality.

The decision to separate chairman and CEO roles should “take into account the firm’s ownership structure and the different tasks embedded in different board roles.”
Goergen, Limbach, and Scholz-Daneshgari (2020) examine the reasons that companies provide for combining the chairman and CEO roles.

Sample: 447 companies (282 dual CEO/chair), 2010.
  – First year companies were required to disclose reason for duality status in proxy.

Most frequent reasons for combining CEO/chairman are unified leadership (56%), CEO knowledge of operations (46%), information flow to board (23%), and the current structure “has served us well” (19%).

Observe negative stock market reaction to “has served us well.” No significant reaction to other main reasons.

Conclusion: market generally accepts leadership and informational benefits of combining roles in companies with dual CEO/chair.
Krause, Semadeni, and Cannella (2013) provide a comprehensive review of the research literature on independent chairman.


Find that the independence status of the chairman has:

1. No consistent relationship with performance.
2. Little impact on managerial entrenchment, organizational risk taking, or executive compensation.

Conclusion: independent chair is not universally beneficial.

Requiring separation “would be misguided, not because the issue of CEO duality is unimportant, but because it is too important and too idiosyncratic for all firms to adopt the same structure under the guise of ‘best practices.’”
CONCLUSION

- The evidence suggests that the independence status of the chairman is not a material indicator of firm performance or governance quality.

- Companies tend to separate the chair and CEO roles to facilitate the succession process, particularly when appointing a first-time CEO.

- Separation might benefit underperforming firms, and harm well-performing firms.

- The market accepts the benefits of dual CEO/chair under certain circumstances.

- Mandatory separation would likely cause more harm than good.


