CHAIRMAN AND CEO : ONE JOB OR TWO?

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There has been an extensive debate over the CEO - chairman duality and separation. While arguments have been presented both for and against, the empirical evidence linking CEO duality with firm performance is limited and inconclusive. Many corporate governance codes and guidelines world over seek to institute independent chairman of the board of directors by recommending a clear division of responsibilities between chairman and CEO of the company. This article presents the prescriptions and practices of separation of chairman and CEO of companies in six major countries of the world including US, UK and India.

The issue of separation of chairman and CEO of company is an important subject of academics and practices not only in developing countries but the developed ones also. The corporate governance reforms which came largely in the wake of the corporate scandals surfacing all over the world, prescribe persistently a clear division of responsibilities between chairman and CEO of the company. Asserting chairman and CEO as two jobs and not one, many corporate governance codes and guidelines seek to institute independent chairman of the board of directors.

The preference for the separate CEO-Chairman is largely grounded in the agency theory of corporate governance concerning the potential for managerial abuse. Finkelstein and D' Aveni (1994) noted, 'duality promotes CEO entrenchment by reducing board monitoring effectiveness'. Cadbury Committee, 1992; Kesner and Johnson, 1990; Lorsch and MarIver, 1989; Rechner and Dalton, 1991, strongly advocated that CEO of the company should not serve simultaneously as chairperson of the board. If chairman and CEO is the same person, it becomes more difficult for the board to provide on independent oversight of management or to evaluate the CEO or to express independent opinion on the management. An independent structure of the chairman is prescribed to facilitate objective assessment of the company and the top management of the company.

On the other side, the practicing managers rarely adopt the view that separation of the two positions is the superior structure (Dobrzynski, 1995; Simison and Bluemenstein, 1995). The practitioners have their

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support in the stewardship theory which suggests that the duality of the CEO and chairman (joint structure) provides unified firm leadership and removes any internal or external ambiguity regarding who is responsible for firm processes and outcomes (Anderson and Anthony, 1986; Donaldson, 1990; Lipton and Lorsch, 1993). Duality offers the clear direction of a single leader, and a faster response to external events. The CEO-cum chairman is expected to have a greater knowledge of the company and the industry, and have greater commitment to the company than a separate chairman.

While the conundrum of CEO duality and separation continues, empirical research linking duality (or separation) with the performance of the firm is inconclusive.[1] Berg and Smith (1978) studied Fortune 200 companies and reported a negative relationship of duality with Return on Investment (ROI), and no relationship with ROE on change in stock prices. Rechner and Dalton(1991) found duality to be negatively associated with ROE, ROI and profit margin. In contrast, Donaldson and Davis (1991) reported that CEO duality was associated with significantly higher levels of ROE.

The next part of the article presents the prescriptions and practices in six major countries of the world including India.

U.S.A

CEO duality is more common in the U.S.A. than other part of the world. Although the current U.S. reforms do not mandate the separation of the roles of Chairman and CEO, they certainly reflect a desire to shift the power centre of the corporation away from the CEO to the Board.[2]

While the Sarbanes-Oxley Act (SOX) addresses issues of managerial and board integrity through a number of provisions[3], the amended listing rules of the NYSE and NASDAQ adopted in Nov. 2003 call for the boards to be comprised of a majority of independent directors and for the non-management and independent directors to hold regular sessions without members of the management present.

Ira M. Millstein has expressed several doubts about the extent to which a CEO is capable of leading the very board that is there to monitor him/ her. Moreover, Millstein and Gregory[4] contend that the board's revised responsibilities require the directors to be better

organised, trained and informed. Such changes increase the need for independent chairman and the amount of time such a chairman will have to devote to board's duties. Since the CEO is already burdened to run the company, it is hard to see how he or she will be able to spend the time and attention needed on board matters.

The National Association of Corporate Directors (NACD) also favours an independent chairman, 'the purpose of creating (an independent) leader is not to add another layer of power but to ensure organisation of, and accountability for, the thoughtful execution of certain independent functions - such as evaluating the CEO, chairing sessions of non-executive directors, setting the board agenda and leading the board'.

Notwithstanding, the trend worldwide of split of chairman and CEO, about 95% of S&P companies in the U.S.A combine the two roles and this proportion has rarely changed in the last 15 years.

U.K.

Sir Adrian Cadbury, chairman of the Committee in the U.K. that looked into corporate governance in the early 1990s emphasised that 'the jobs of chairman and chief executive demand different abilities and perhaps temperaments. It is very much in shareholder's interests to ensure they are performed by different people'. [5]

Hermes in the U.K. which published it statement on Corporate Governance and Voting Policy in July 1998 also advocated separation of the post of chairman and chief executive. Higgs report in 2002 to review combined code of U.K. also reiterated the separation of the roles of chairman and chief executive and clear division of responsibilities between the two in writing. Further, it cautioned against a chief executive becoming chairman of the same company.

The Revised Combined Code which is applicable (on and after Nov. 2003) to U.K. listed company as the Voluntary Code of Corporate Governance on 'comply or explain' basis, include the main principle (A.2) which states that the roles of chairman and chief executive should be split and further a chief executive should not go on to become chairman of the same company.

There is a high level of compliance in the U.K., particularly among larger listed companies of the principle of separation of the two roles. As per the Higgs Report, 2003, the percentage of companies with joint chairman/ chief executive (i.e. not complying with the principle) were as follows.

	Company Type	% of companies not complying
(i)	FTSE 100 (largest 100 listed companies)	5
(ii)	FTSE 250 (largest 101-350 listed companies)	8
(iii)	Other companies listed on the stock exchange	11
(iv)	Average	10

AUSTRALIA

The listed companies in Australia are regulated by the listing rules of the Australian Stock Exchange (ASX), which are mandatory. The ASX listing rules recommend a clear allocation of functions between the board of directors and management of the company. The listing rules require the chairman of the company to be an independent non-executive director, and if the chairman is not an independent director, there should be a 'lead independent director'.

Australian listed companies generally have a unitary board structure with a balance of executive and non-executive directors and a separate chief executive and chairman. Non-Executive Directors and Chief Executives Remuneration and Board Governance Survey Report 2002 indicate an increasing trend in Australian companies to separate the chief executive and chairman. It was reported that in 2002 89% of all boards had a non-executive chairman against 85% in 1999.

JAPAN

The structure of the board of directors in Japan is the traditional unitary board where important decisions need action by the entire board. Theoretically, in Japan board of directors has the ultimate authority to oversee the functioning of the company on behalf of the shareholders, in practice, however, the boards have surrendered most of their authority to the company president.[6] The power of governance in Japanese companies is concentrated in the company president and an operating committee of top executives which

evaluate the performance of the company against its goal and also select new board members and officers.

The Japanese model of corporate governance is a 'network model' (Moerland, 1995) wherein the reality of power lies in the personnel relationship which the president maintains with business associates, banks and government officials.

GERMANY

The German corporate structure for companies is based on a two-tier system wherein, the governance of the company is shared by two boards: the executive board (*Vorstand*) charged with the executive function of the company, and the supervisory board (*Aufsichtsrat*) to oversee the executive board. The executive board consists entirely of full time managers. The supervisory board consists of both full time employees (usually ½ - elected by the employees) and of non-executive outsiders such as representatives from banks, professional advisors to the company.

The CEO is usually a member of the supervisory board but the chairmanship goes to a senior member of the board (mostly representative of the lead bank), who does not have any executive role in the company. Thus, the two positions are quite separate in Germany.

INDIA

The Indian codes of corporate governance viz. CII code, Clause 49 of the Listing Agreement, Revised Clause 49 while silent on the issue of separation of chairman and CEO, link independent (non-executive) chairman with the component of independent directors in the board of directors of company. The CII report recommended that if the chairman and CEO (or Managing Director) is the same person, independent directors should constitute 50% of the board, and 30% of the board in case the two positions are separate.[7]

The Kumar Mangalam Birla Committee's views on the subject were quite ambiguous. The committee was of the opinion that the chairman's role should in principle be different from that of the chief executive, though the same individual may perform both the roles.[8] In the mandatory category of recommendations, the committee dittos

the CII recommendations of linking non-executive chairman with the composition of board of directors of the company. The same provision was incorporated in Clause 49 as well reiterated in the Revised Clause 49 of the Listing Agreement by the SEBI.

As a non-mandatory recommendation, the Committee recommended that a non-executive chairman (in case it is there) should be entitled to maintain a Chairman's office at the company's expense and also allowed reimbursement of expenses incurred in performance of his duties.

The Indian approach different from many codes and guidelines elsewhere is not unique. The Malaysian Report on Corporate Governance, for example, similarly, emphasized that 'where the roles (Chairman and CEO) are combined, there should be a strong independent element on the board.

PRACTICES IN INDIA

In most of the public sector companies especially banks, the designation CMD i.e. Chairman cum Managing Director is quite common. In the private sector, it is not uncommon to find companies where the chairman (non-executive) has been the CEO of the company prior to assuming the new responsibility. Take the case of Tata Motors (of Tata Group) where Mr. Ratan Tata was the Executive Chairman of the company till sometime back. On attaing 65 years of age, he relinquished the post to become non-executive chairman with no MD/CEO in the company for quite a number of years.[10]

In the top 500 companies listed on the Bombay Stock Exchange, the practice discernible[11] is that more than 50% of the companies have a separate chairman of the company. Of the multi-national corporations (MNCs), more than 80% of the companies in India have an independent chairman. This position is reversed in public-sector undertakings (PSUs), where more than 70% of the companies have a chairman cum managing director (CMD) with nearly 100% in public sector banking companies. A mixed trend is observed in companies controlled by family groups in India, where the independent chairman of the company has little significance as in most cases chairman and MD are different persons on record but not independent (as they are family members) e.g. Hero Honda Motors,

Mahindra and Mahindra, Munjal Son's, Thapars, to name a few. There are many instances in family group companies where the CEO of the company has risen to take over as the chairperson of the same company. Thus, the linking of independent component of directors in the board of directors with the independence of the chairman of the company (non-executive chairman) in the corporate governance code laid down in India is inconsequential. Since the Indian corporate sector is dominated by companies controlled and managed by family groups[12], the structure of the chairman and CEO should be designed to deal with this specific Indian situation.

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For example, additional authority and responsibility to audit committee, adoption and disclosure of code of ethics for CEO and CFO, certification by CEO and CFO etc.

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ibid para 8.2.

Till it is conferred on Mr. Ravi Kant

Based on author's calculation (Source : Directory of BSE 500, BSE, Mumbai).

For example, 17 of the 30 Sensex companies are family - controlled.

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MICROFINANCE : A TOOL TO SOCIO-ECONOMIC DEVELOPMENT FROM BELOW?

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Economic growth is not meaningful unless it is inclusive. For achieving inclusive growth, access to financial services is a critical precondition. This is where the growth of financial sector will help the nation greatly. Development of microfinance sector is one of the important means for facilitating financial inclusion. The Indian microfinance market is growing and evolving extremely quickly. With these changes come challenges which the microfinance sector is facing or may face if certain remedial actions are not taken timely. Based on a selective literature review, this paper appraises the role of microfinance in the empowerment of people and the realisation of financial inclusion in India. It is a common practice to look upon microfinance as a valuable tool for alleviating povert, but this paper attempts to look at the flipside of microfinance and offers a critique of some of its characteristics. Some of the practices that are followed by certain microfinance institutions (MFIs) do not seem to be appropriate. The lack of transparency, ill-designed products, inadequate communication with the clients and unfriendly methods of recovery are not consistent with the objectives of serving the poor. Microfinance is a great tool as a survival strategy, but it is not a magical solution to end poverty and promote development. Yet, in all the hype we have forgotten to question the basic premise. Is lack of credit the only problem? Or one of the many problems the poor face? If the latter is true, then the credit provision will be effective only when it is delivered after other barriers have been removed.

I- Microfinance: Meaning And Issues Of Concern

Microfinance is the method of credit delivery to the poor. According to an accepted definition, microfinance is provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi urban or urban areas for enabling them to raise their income levels and improve living standards.[†] Loosely defined, microfinance is the giving of very small amounts of credit and financial services and assistance to the poor people at low rate of interests, with no collateral, who are ignored by most institutional credit systems, to help them raise their income levels and living

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† http://www.nabard.org/pdf/publications/reports/mF_Scenario_in_the_Country.pdf (accessed 1 Aug 2009).