



Paul Davis

# How to **separate** the roles of chairman and CEO

*Many companies that thought they knew how to split them stumbled along the way. Five steps can make the process smoother and more successful.*

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**US companies are increasingly** separating the roles of the chairman and the chief executive officer. Boeing, Dell, the Walt Disney Company, MCI, Oracle, and Tenet Healthcare have all done so during the past year, and a new study finds that roughly one-third of US companies have adopted such a split-leadership structure, up from a historical level of about one-fifth.<sup>1</sup>

Yet while more companies—in the US and elsewhere—agree that separating the two roles makes sense, many are less sure about the best way to proceed. This uncertainty results in part from the polarized opinions of key stakeholders about whether to separate the roles in the first place and in part from the absence of widely disseminated best practices. For instance, company directors and investors in the US seem to support splitting the roles—hardly surprising, given the mounting pressure on boards to become more independent of management—but CEOs are understandably less certain.<sup>2</sup>

Experience from the United Kingdom, which has experimented with the split model for more than a decade, indicates that companies should move deliberately and judiciously. What may seem like a straightforward

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<sup>1</sup>Based on a September 2004 study of more than 2,500 companies across the world by Governance Metrics International, the New York-based corporate-governance ratings agency.

<sup>2</sup>Robert F. Felton, “What directors and investors want from governance reform,” *The McKinsey Quarterly*, 2004 Number 2, pp. 30–9 ([www.mckinseyquarterly.com/links/15020](http://www.mckinseyquarterly.com/links/15020)). While this debate will play out over time, many companies have decided to embark on such a change. This article is intended to guide these corporations through this process.



change of roles is actually a complicated process influenced by unpredictable factors—especially the personal interactions of the two people chosen for the posts. The switch requires careful planning and can take years to execute smoothly. Many companies thought they were doing well, only to stumble along the way.

Take the British retailer Kingfisher, whose chairman-CEO Geoffrey Mulcahy relinquished the chief executive role in 1993 to Alan Smith, recruited from the retailer Marks

and Spencer. Investors, figuring that Mulcahy's famed strategic thinking would dovetail nicely with the retailing skills Smith had honed during 27 years at M&S, applauded the move. However, Smith had difficulty adjusting to Kingfisher's more entrepreneurial and decentralized culture. After two years, when it had become obvious that the men's poor working relationship had contributed to a string of bad financial results, the board took action, showing Smith the door. Mulcahy was named CEO with a charge to fix Kingfisher's many problems, while nonexecutive director Nigel Mobbs became acting chairman. "There was a duplication between Geoff Mulcahy and Alan Smith, and this I think led to confusion," concluded Mobbs at the time.<sup>3</sup>

Boards bear the ultimate responsibility for making the split work. Experience suggests that five things are required to manage it in a smooth and orderly way: identifying the right board members to lead the process, determining the best form and timing for the separation, defining suitable roles for the chairman and the CEO, appointing an appropriate person to each post, and fostering a productive relationship between the two. Some of this article's recommendations, drawn primarily from experience in the United Kingdom, may seem intuitively obvious, but companies ignore them at their peril.

### Leading the process

Since boards bear responsibility for the outcome of the process, they ought to lead it and choose the candidates.<sup>4</sup> But it's not a good idea to

<sup>3</sup>Jane Merriman, "Top executives to leave Britain's Kingfisher," Reuters, January 27, 1995.

<sup>4</sup>If the board has no governance or nominations committee, the process should be led by independent members under the stewardship of the lead independent director, if any.

include all board members. The board's governance (or nominations) committee, which should consist of only independent directors, ought to take the lead, while board members who are executives of the company probably ought to recuse themselves, since otherwise they would be choosing their own bosses.

Similarly, the independent directors should conduct the process at some distance from the current chairman-CEO, particularly if he or she hopes to retain one of the roles after the split. Even a current boss who supports the separation is likely, perhaps unconsciously, to propose candidates who would follow the strategy and policies he or she put in place. While that may not seem like a bad thing, particularly if business is good, a more detached assessment of the company's direction and leadership is usually preferable. In the later stages of the process, the entire board should become involved to ensure that the people chosen as chairman and as CEO have the support of all the directors.

### **Right form, right timing**

When US companies split the roles of chairman and CEO, the current holder of the combined position typically cedes only one title rather than depart altogether. Experience in the United Kingdom, however, suggests that companies may be better off when the boss gives up both. In the mid-1990s, as UK boards followed the recommendation of the Cadbury Code of Best Practice to split the roles, some chairmen-CEOs gave up the chief executive's job but stayed on as chairman. UK companies that adopted this approach concluded that it wasn't workable.<sup>5</sup> As in the Kingfisher case, the chairman's resistance sometimes made it hard for a new CEO to institute changes. At other companies, executives were confused about where to place their loyalty and who should give them their orders. Similar problems would arise if a chairman-CEO gave up the chairmanship but continued to serve as chief executive. In this case, the new chairman could be less effective because the current directors might continue to view the CEO as the real leader. Furthermore, a chief executive used to running the show as chairman-CEO may not be willing to take direction from a new chairman or to accept the board's authority. So the UK Combined Code (the successor to the Cadbury Code) states that a chairman should be independent at the time of appointment, and more than three-fourths of the United Kingdom's 100 largest publicly traded companies now have a chairman who wasn't formerly the chief executive.

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<sup>5</sup> John Roberts, *On Becoming Company Chairman: Building the Complementary Board*, London: Saxton Bampfylde Hever, 2000 ([www.saxbam.com](http://www.saxbam.com)).

Some US companies too have learned this lesson the hard way. The chairman-CEO at one of them ceded the role of chief executive only to reclaim it after undermining the new CEO's authority and making it difficult for him to win the employees' attention when the person they considered to be the ultimate boss was in the room. In a minority of cases, a chairman-CEO was successful as chairman after ceasing to be CEO, but only because he or she genuinely relinquished that role, slowed down, and stepped out of the limelight by consciously steering clear of management responsibilities. Intel chairman Andy Grove said that dropping the role of CEO was one of the most difficult transitions in his life but that he learned in this way to control a tendency to dig into details and dominate decision making.<sup>6</sup> Another US chairman who previously wore both hats says that when employees turn to him for management guidance, he routinely refers them to the new CEO, even if he himself has the answer.

*More than three-fourths of the **100 largest** UK public companies now have a chairman who wasn't formerly the chief executive officer*

A substantial amount of time could be needed to effect the separation. In some cases, a company crisis may prompt directors to initiate it and to hire new leadership quickly. For the most part, however, boards have the

luxury of time to seek out the right people for the two posts. The UK defense contractor BAE Systems, for instance, took more than a year to find a replacement for the outgoing chairman, Dick Evans, because of the

industry's highly specialized nature. In the United States, given the lack of precedents and the potential reluctance of candidates to accept the split, even more effort may be required to get the right nonexecutive chairman.

The best way to proceed is to make the division of the two roles an integral part of a company's succession planning. As a McKinsey poll shows, US chairmen-CEOs will probably resist ceding power.<sup>7</sup> To avoid disruption that could harm their motivation and performance, particularly at top companies, boards may wish to wait until they leave before instituting a divided model. In the interim, the governance committee could appoint a lead independent director, who might be groomed as the next chairman.

Companies can also choose to stagger the separation of roles. At one European bank, for instance, the board developed a 15-month plan for the switch: First, a special committee would spend about six months

<sup>6</sup>Brent Schlender, "Inside Andy Grove's latest crusade," *Fortune*, August 23, 2004.

<sup>7</sup>Robert F. Felton, "What directors and investors want from governance reform," *The McKinsey Quarterly*, 2004 Number 2, pp. 30-9 ([www.mckinseyquarterly.com/links/15020](http://www.mckinseyquarterly.com/links/15020)).

to come up with the desired CEO profile and to undertake a broad search. Once the CEO had been appointed, he or she was to work with the former chairman-CEO, who would serve as chairman during a 9-month transition. When this period came to an end, the chairman would relinquish his job to a nonexecutive director. At the US company Waste Management, the chairman-CEO, A. Maurice Myers, relinquished the CEO role to David P. Steiner, who was the company's chief financial officer, in March 2004. When Myers retires as chairman, nonexecutive director John C. Pope is slated to succeed him.

### Defining the roles

One important and often overlooked task for the governance committee is to define the very different but complementary jobs of the chairman and the CEO, thereby reducing the possibility that overlapping roles will generate conflict between them. The natural starting point is for the committee, in conjunction with the entire board, to define the roles of the board and of management. Boards, at a minimum, must fulfill their oversight responsibilities under the law. But many want to go further by acting as adviser and coach to the CEO, by contributing in a meaningful way to the development of the strategy and talent of the company, and by helping to manage its performance. Every board must determine the specific role it wants to play and then agree with management on their respective functions. Clarity on this front will ensure that only candidates who complement the board receive consideration for the posts of chairman and of CEO.

#### EXHIBIT I

#### Clearly define the roles

Chairman	CEO
<b>Overall responsibility</b>	
<ul style="list-style-type: none"> <li>• Ensure board sets and implements company's direction, strategy effectively</li> </ul>	<ul style="list-style-type: none"> <li>• Responsible for performance of company as dictated by board's overall strategy</li> </ul>
<b>Specific duties</b>	
<ul style="list-style-type: none"> <li>• Provide leadership to board               <ul style="list-style-type: none"> <li>– Plan board meetings, agendas</li> <li>– Ensure board receives proper information</li> <li>– Chair all board meetings</li> <li>– Ensure that all directors contribute</li> <li>– Drive discussion toward consensus</li> </ul> </li> <li>• Determine composition, structure of board</li> <li>• Chair shareholders' meetings</li> <li>• Act as company's lead representative: explain aims, policies to outside world</li> </ul>	<ul style="list-style-type: none"> <li>• Develop, implement strategy reflecting long-term objectives, priorities established by board</li> <li>• Assume full accountability to board for all aspects of company operations, performance</li> <li>• Maintain ongoing dialogue with board chairman</li> <li>• Build, maintain effective executive team</li> <li>• Put adequate operational-planning, financial-control systems in place</li> <li>• Closely monitor operating, financial results in accordance with plans, budgets</li> <li>• Represent company to major customers, professional associations</li> </ul>

Source: Institute of Directors (UK)

Once the board’s role has been defined, the committee can turn to the roles of the chairman and the CEO, starting from the principle that the chairman runs the board, determines its priorities, and sets the agenda for meetings—all with input from the CEO—while the CEO manages the company and is accountable for corporate performance (Exhibit 1, on the previous page). A chairman shouldn’t undertake management responsibilities (for instance, operational roles), and a CEO shouldn’t attempt to run the board. A division is necessary because one important reason for splitting the two jobs is the desirability of making the board more independent. A chairman with an operational role would in effect be a part of management and therefore less independent from it.<sup>8</sup>



As the committee designs the chairman’s duties, it should also spell out the involvement and time commitment required to hold the position (Exhibit 2)—a point that may seem trivial but actually plays an important part in differentiating the two roles (see “Splitting chairs: Should CEOs give up the chairman’s role?” in the current issue). In the United Kingdom, chairmen typically spend about two days a week on the job, which reduces the likelihood that they will intrude upon management activities. Of course, a chairman may need to make a greater commitment if the company is young, lacks management depth, or is undergoing a major transformation or crisis.

The committee can best delineate the roles by developing a comprehensive, written job description for each of them.<sup>9</sup> These documents, which are much more than just a formality, facilitate the search process by telling job candidates what to expect and leaving less room for surprise. They also guide the relationship between the chairman and the CEO once the appointments have been made and reduce the risk that either will attempt to overreach. “It is precisely because there is so much common ground

<sup>8</sup>James J. Darazsdi and Robert B. Stobaugh, *The Governance Committee: A Director’s Handbook*, Washington, DC: National Association of Corporate Directors, 2003. As the authors put it, “Who leads the board in ensuring effective board governance? The answer should point to an independent director.”

<sup>9</sup>The UK Combined Code recommends as best practice the development of written job descriptions, accepted by the board, for both posts. But a survey that Market & Opinion Research International (MORI) conducted for the Higgs Report, which was commissioned by the UK government in 2002 to assess the effectiveness of nonexecutive directors, found that only 53 percent of the 72 UK chairmen in the survey had been given specific objectives to fulfill their role.

## EXHIBIT 2

How much involvement is required?		
Issues facing board	Chairman's role	
	Light	Heavy
Corporate strategy	<ul style="list-style-type: none"> <li>• Strategy defined, well understood (internally and externally)</li> <li>• Company is simple/single business entity</li> </ul>	<ul style="list-style-type: none"> <li>• Complex, diverse portfolio</li> <li>• Major strategic reorientation required; company is new or in transition</li> <li>• Recent/pending merger or acquisition</li> </ul>
Management issues	<ul style="list-style-type: none"> <li>• Experienced CEO, management team in place</li> <li>• Strong rapport, trust, and confidence between CEO and board</li> </ul>	<ul style="list-style-type: none"> <li>• New or inexperienced CEO, management team</li> <li>• Significant upgrade in management capabilities needed</li> </ul>
Shareholder value/corporate performance	<ul style="list-style-type: none"> <li>• High corporate performance</li> </ul>	<ul style="list-style-type: none"> <li>• History of poor performance management</li> <li>• New performance standards required</li> </ul>
Other governance issues	<ul style="list-style-type: none"> <li>• Established board in place</li> <li>• Culture aligned with strategic objectives</li> </ul>	<ul style="list-style-type: none"> <li>• Undefined governance, leadership structure</li> <li>• Strong cultural legacy requiring transformation</li> </ul>

between the two posts that the mapping of the respective territories should be the starting point,” says Adrian Cadbury, whose eponymous guidelines launched the separation of the roles in the United Kingdom.<sup>10</sup>

### Appointing the right people

The most important contributors to the success of any split-leadership structure, of course, are the chairman and the CEO themselves. To identify the right people, boards should assess not only the technical skills of the candidates but also the way their mental dispositions mesh—or fail to mesh.

For chairmen, the most important characteristic—over and above the usual ones, such as integrity and leadership ability—is a lack of ambition to be CEO: only someone content to serve in a secondary, behind-the-scenes role can have a productive and trusting relationship with the chief executive. The lack of rivalry fosters cooperation, eases the flow of information, and helps chairmen to serve as effective mentors to CEOs and to revel in their success.

A willingness to ease into the background requires a degree of humility that is perhaps unusual for anyone who has climbed so high. At a

<sup>10</sup> Adrian Cadbury, *Corporate Governance and Chairmanship: A Personal View*, New York: Oxford University Press, 2002.

leading UK food and beverage company, the chairman occupies a small, nondescript office to let employees and others know that he doesn't run the company. In contrast, the chairman of a prominent US company continues to occupy the same spacious office he had when he was also the CEO, which may suggest to employees that he still runs the company rather than just the board. One UK chairman described the difficulty of making the transition:

There is a process of withdrawal. You're used to being famous and in demand all the time, both internally and externally. You're used to being the boss. All these things are drugs. In a sense, it's the end of an ambition that's been around a long time—to be a success as a CEO—and all of a sudden you're not going to be one anymore. There is loss and grieving. But then you come to the realization that what you've taken on is more than you thought it was and you say, "Well, am I ambitious to become a good chairman?" and it's the start of something different.<sup>11</sup>

In the United Kingdom, many chairmen are former CEOs of other companies who, having already climbed to the commanding heights of management, are now happy to play a less visible, supporting role. They are often a decade or so older than their CEOs, and this age gap seems to enhance their ability to serve as mentors. In the United States, a few companies appear to be replicating this pattern.

Often the chairman comes from the ranks of the company's current non-executive directors—ideally, one who has served on the board for several years and knows the business well. This two-step path to the chairmanship is gaining broader acceptance. The board of GlaxoSmithKline, for instance, appointed Christopher Gent as an independent director earlier this year with a view to having him succeed Christopher Hogg as chairman at the end of it.

Like finding the right chairman, finding the right CEO can be a delicate problem. Over and above the intellect and drive needed to manage a company, a chief executive must have a healthy respect for the authority of the chairman and the full board. That may be a tough pill to swallow for a CEO—especially a former chairman-CEO—who is accustomed to a hands-off attitude on the part of the board. Indeed, this kind of resistance is one reason for requiring holders of the combined position to

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<sup>11</sup> John Roberts, *On Becoming Company Chairman: Building the Complementary Board*, London: Saxton Bampfylde Hever, 2000 ([www.saxbam.com](http://www.saxbam.com)).

relinquish both roles. The chief executive controls key corporate resources and often regulates the flow of important information to outside directors. A CEO who isn't a collaborative partner with the chairman can have extremely bad relations with the board and undermine its effectiveness. Any CEO candidate who isn't willing to work cooperatively with the board and the chairman should therefore be eliminated from consideration. As former ICI chairman Denys Henderson has said, "The success of the nonexecutive-chairman arrangement is heavily dependent on the chairman's relationship with the CEO. If the chemistry isn't good, the relationship isn't going to work. And if the relationship does not work, the board and the company

are in serious trouble."<sup>12</sup> It is thus important to ensure that the chairman and the CEO have complementary skills, styles, and personalities.

### Recommended reading

Readers who wish to investigate more deeply the issues discussed in this article should consult the following works:

- Adrian Cadbury, *Corporate Governance and Chairmanship: A Personal View*, New York: Oxford University Press, 2002.
- Terry McNulty, John Roberts, and Philip Stiles, *Creating Accountability Within the Board: The Work of the Effective Non-Executive Director*, London: Department of Trade and Industry ([www.dti.gov.uk](http://www.dti.gov.uk)). This report for the 2002–03 Review of the Role and Effectiveness of the Non-Executive Director, which led to the July 2003 revision of the UK Combined Code, was conducted by Derek Higgs, the former chairman of S. G. Warburg and a current non-executive director at a number of UK companies.
- John Roberts, *On Becoming Company Chairman: Building the Complementary Board*, London: Saxton Bampfylde Hever, 2000 ([www.saxbam.com](http://www.saxbam.com)).

How to encourage good chemistry? Directors at a struggling UK company recently asked the CEO to participate in the final stage of selecting a new chairman. Armed with a headhunter's short list of outside candidates, the board met with each of these people and asked the CEO to meet them as well. The board assured him that it would remove candidates from consideration if he anticipated any difficulty working with them. Eventually it hired a turnaround specialist who had extensive experience as a chief executive but was ready to step back and take a nonoperating role.

### Fostering positive relations

Once the chief executive and the chairman are in place, it is largely up to them to develop an effective working relationship—building trust, ironing out differences in styles, and allocating shared responsibilities. Experience in the United Kingdom

<sup>12</sup> "Redraw the line between the board and the CEO," *Harvard Business Review*, March–April 1995, pp. 187–212.

has shown the importance of establishing a regular communications routine through phone calls, e-mails, and face-to-face meetings to let information flow and provide a context for collaboration.

One common initial step is for the chairman and the CEO to agree on their respective roles. Even where job descriptions exist, they usually don't cover all aspects of the work—particularly how to share responsibility for the development of strategy. “The agreement [between the two] should be put down in writing and eventually approved by the board,” says Henderson. “But the process of thoroughly understanding each other's viewpoint is more important than the final text.”<sup>13</sup>



Candor is a key ingredient for making the relationship work: Misunderstandings can create a vicious cycle of suspicion that eventually spirals into open distrust and acrimony. The CEO, who has an advantage in controlling information about the company, must demonstrate a willingness to share all news, good and bad, with the chairman, who should clearly proclaim a desire to avoid day-to-day decision making and give other nonexecutive directors adequate opportunities to spend time with the CEO. Such opportunities are important because they help nonexecutive directors to participate meaningfully in the board's work, and an excessive focus on the relationship between the chairman and the CEO might alienate the other board members.

Whatever the difficulties, many boards have smoothly separated the two roles and chosen leaders who meshed together well in them. Take BP, which adopted the split model in 1992, when the board responded to plummeting profits and high debt by forcing out the chairman and CEO, Robert Horton; making David Simon, then the chief operating officer, his successor as chief executive; and appointing the outside director and former Barings chairman Lord Ashburton as part-time chairman. The pair restructured the company radically, selling assets,

<sup>13</sup> “Redraw the line between the board and the CEO,” *Harvard Business Review*, March–April 1995, pp. 187–212.

reducing capital spending, and laying off staff. Simon focused on the internal reorganization, instilling discipline, teamwork, and a performance-oriented culture. Ashburton served as BP's statesman in the outside world and contributed his financial expertise. The turnaround was rapid. In mid-1995, when the company had record share prices and surging profits, Ashburton retired and Simon became chairman.

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Deciding to separate the roles of chairman and CEO is only the first step in a process fraught with hazards. Much hinges on personal interactions, which are hard to predict, and problems are bound to arise during the transition. But boards that identify the potential pitfalls and develop strategies to avoid them are much more likely to achieve a smooth separation. *Q*

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