Job Split Doesn't Always Work Magic

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Efforts to split the posts of chairman and chief executive at U.S. companies are finding success. Now all that is needed is evidence it actually helps investors.

Studies show a mixed impact on shareholder returns when independent chairmen are named to keep a better eye on CEOs. While the evidence suggests a split could help companies that are struggling, it also shows the step could hurt shareholders in many other cases.

An apparent power struggle at Occidental Petroleum Corp. and activists' push for J.P. Morgan Chase & Co. to split the roles have sharpened the focus on the issue this spring. Advocates argue separating the jobs leads to better corporate governance by putting a more formal check on CEO power. But the studies do raise questions about whether and when it makes sense to force a split.

A study by Ryan Krause and Matthew Semadeni at Indiana University's Kelley School of Business found that splitting the chairman and CEO jobs at 309 U.S. companies from 2002 to 2006 helped if the company was struggling but hurt if it was performing well.

Specifically, their analysis predicts that if a CEO is stripped of the chairman's job in a year when a company delivers a total shareholder return of negative 30%, the company would deliver a positive 42% return the following year. But if the roles are separated in a year when a company books a positive 30% return, the next year the company would post a negative return of 42%.

"In the end, these issues boil down to the old truism, 'If it ain't broke, don't fix it,' " wrote the authors of the study, which is to appear in the Academy of Management Journal in June. "Boards implementing this change under such circumstances risk reversing strategies and systems that are currently producing superior returns."

That reasoning could argue against a split at J.P. Morgan, where shares have risen about 20% in the past year.

J.P. Morgan Chairman and CEO James Dimon is campaigning hard with investors to defeat a nonbinding resolution to separate the jobs. The resolution comes up for a vote at the bank's May 21 annual meeting and has won the support of proxy advisers Institutional Shareholder Services and Glass, Lewis & Co.

A similar proposal won 40% of the vote at J.P. Morgan's annual meeting last year. Overall, such resolutions won an average of 35% of the vote in 2012, according to ISS. Mr. Dimon told Sanford C. Bernstein analysts that he hopes to remain at the bank "for many years to come," according to a note they posted after a private meeting.

A 2009 review of studies on independent chairmen by the Millstein Center for Corporate Governance and Performance concluded the impact on performance "was inconclusive," said

Stephen Davis, associate director of Harvard Law School's programs on corporate governance and institutional investors, who helped oversee the review.

"It isn't driven by research," Mr. Davis said of the push to separate the top two jobs. "It's driven by investors' views about accountability."

A company's stock returns depend on a lot of factors beyond the way it is managed. Cyclical or longer-running trends in the underlying business, strategies pursued by competitors, and the strength of the economies where a company does business each play a role.

Advocates of an independent chairman say it is the right thing to do wherever it fits into that mosaic. Splitting the top two roles can improve decision making, cut back on risky behavior and better divide labor, they say, points echoed by people who have held such jobs.

"When you have an independent chairman, directors are more willing to have a candid discussion of opposing points of view," said Harry Pearce, a retired General Motors Corp. vice chairman, who has been the independent chairman of energy company MDU Resources Group Inc. since 2006. "Sitting at the head of the table and having control over the agenda is very consequential."

Terry Hildestad, who worked with Mr. Pearce as CEO of MDU until he retired in January, said having a separate chairman made things easier for him during the 2008-2009 downturn. "We had massive layoffs," he said. "I focused on managing the company and operating the business units and did not spend significant time managing the board. Harry did."

Years ago, U.S. CEOs almost always held the job of board chairman, a position that otherwise would carry the responsibility of monitoring the CEO's performance on behalf of shareholders and planning for succession. The positions are commonly split in countries like the U.K., however. A string of accounting scandals more than a decade ago started to turn the tide in the U.S., and pressure from investors and regulators in the wake of the financial crisis led many companies to split the roles.

As of June 2012, 21% of Standard & Poor's 500 companies had an independent board chairman, up from 19% in 2011, according to ISS. At other companies in the index, departing CEOs stayed on as chairmen to groom successors.

GMI Ratings, a corporate-governance research firm, looked at the impact of splitting the top jobs on shareholder returns and other considerations in a study published last June.

The research found total shareholder return at companies where CEO and chairman posts were combined outperformed those where the positions had been separated after one year (returns of 12% compared with 2.3%) and after three years (returns of 104% compared with 95%). The reverse was true after five years, when companies with split roles returned 40% and companies with combined roles returned 31%. The figures track appreciation in share price plus reinvested dividends.

"One possible reason is that a CEO unopposed by an independent chairman may find more freedom to make decisions in a way that immediately benefits the company," authors Paul Hodgson and Greg Ruel wrote. "These aren't always the decisions, however, that lead to a successful long-term model."

Companies with split roles pay CEOs and chairmen less and take fewer accounting-related risks, the study found. A separate 2009 study by the Corporate Library, a research firm that later merged with GMI, found that businesses with a single CEO-chairman tend to have less frequent board meetings and staggered director elections, which make it harder to mount proxy fights.

The lack of persuasive evidence of improved returns doesn't bother Gary Wilson, a former independent chairman of Northwest Airlines Corp.

"Anybody who says there's not a study, I say, 'So what?' This is common sense,"' Mr. Wilson said. "There are a million things that can affect shareholder returns and any number of things that are more important than a separate chairman and CEO."