

# CEO Duality and Board Independence

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## Abstract:

In modern corporations, the board of directors represents the shareholders. Board of directors are responsible for setting corporate direction and ensuring corporate performance even as it monitors the conformance of company executives to the policies and programs it has laid down (Collis and Montgomery, 1998; Tricker, 1994). Even as ultimately the responsibility for company performance lies with the CEO; starting with the establishment of purpose translated into strategies and implementing such by providing leadership and creating an ethical as well as a challenging work environment, the board is still accountable to the shareholders for maximizing returns on their investments (Collis and Montgomery, 1998). While the board monitors the CEO and may fire him in cases of poor performance, this role of the board becomes challenged when the board chairman is the CEO as well. Still, CEO duality abounds in the Philippines.

This paper looks into the relationship between board independence and CEO duality. The study is informed by two perspectives. Duality and the issue of corporate governance in general are commonly viewed from the perspective of agency theory (Canyon and Peck, 1998; Sanders and Carpenters, 1998; Beatty and Zajac, 1996). However, in addition to agency theory, this paper uses institutional theory in explaining duality. The two theories taken together, one anchored on the assumption that organizations adopt structures that maximize efficiency and another based on the assumption that organizations adopt structures that increase legitimacy regardless of efficiency concerns, provide additional insight on the nature of duality (Palmer, Jennings & Zhou, 1993; Gooderham, Nordhaug & Rongdal, 1999).

From the agency theory perspective, the board of directors protects shareholders from top management actions that are not congruent with their interests. Such problems arise because of the separation of ownership of the firm from its management (Fama and Jensen, 1983). But by separating the control of decisions (ratifying and monitoring) from its management (initiating and implementation) agency problems may be mitigated (Fama and Jensen, 1983). On the other hand critics advance that, separating the positions of chairman of the board and CEO weakens the CEO's authority and dampens his entrepreneurial spirit, which is critical to a company's survival (Collis and Montgomery, 1998). The presence of dual and non-dual CEOs tells us that perhaps there may be conditions that make for the existence of duality.

Another perspective that may shed light on duality is institutional theory. From this perspective, organizations are seen as operating in a social network of relationships. As such, the organization adopts governance arrangement that does not necessarily maximize efficiency rather, legitimacy (Palmer, et al., 1993). When an organization becomes accepted in its network, it gains legitimacy, which increases its chances for survival (Di Maggio and Powell, 1983). One of the ways in which legitimacy is gained is through isomorphism, the organization's resemblance to others in its environment. It is also advanced that isomorphism increases legitimacy (Deephouse, 1996; Di Maggio and Powell, 1983). Di Maggio and Powell (1983) stated that isomorphism may result from three pressures: coercive pressures which result from political factors or government mandate, mimetic changes which are an organization's response to uncertainty, and normative pressures arising from professionalism and social networks. In addition, legitimated arrangements may be perpetuated through tradition, which may be exemplified by the founding members of the network (Palmer, et al., 1993). Thus from this perspective, duality may be a function of an organization's effort to gain legitimacy as it resembles other organizations in its field.