Changing Scenes In, From and Outside the Board Room: UK corporate governance in practice from 1989 to 1999[1]

Annie Pye*

This paper is about changes in 'corporate directing', observed from interviews spanning the last ten years with Chairmen, Chief Executives, executive and non-executive directors in nine large UK organizations. Not only has the economic, political and social context changed, the 'what', 'how' and 'why' of boards has also changed. This paper seeks to illustrate some of these changes, both inside and outside the board room, where the role of fund managers has also changed. It concludes that the Chairman and Chief Executive relationship provides a powerful axis around which board room culture (r)evolves and corporate govern*ing* takes place.

Introduction

This paper aims to contribute to the needs identified by Tricker (1999) for further descriptive studies of corporate governance and by Pettigrew (1995) for in depth, longitudinal study of boards. Funded by ESRC, in 1987–89 we studied Chairmen, Chief Executives and executive team members in twelve large UK organizations: Avon Rubber, Beazer, BTR, Coats Viyella, Glynwed, Hanson, Lucas, Marks and Spencer, Metal Box, Prudential, Reckitt and Colman and TSB (Mangham and Pye, 1991). In 1997–2000, we were funded again by ESRC to return to these contributors and to their 'current equivalents' in these organizations (as far as we were able to identify them), effectively with the same question: how do you 'run' a large organization?

A host of significant changes in the corporate, political, social and economic world of the intervening decade creates a very different context in which executive managing or corporate directing now takes place. Likewise, actual practice also appears to have changed. Phrases such as 'strategic focus', 'shareholder value' and 'corporate governance' are common to almost every 1999 interview but were entirely absent from our 1980s data although undoubtedly all contributors at that time would have claimed to be running strategically directed, profitable and ethically sound enterprises. Our work aims to elaborate some of the what, how and why questions which underpin these apparent changes in board practice.

The first section of this paper will draw a brief sketch of the contemporary context in contrast with that of ten years ago. The next section will locate the current study in this context and summarise some early findings, focusing on the inter-related themes of *how* boards work, Chairman and Chief Executive (CE) relationships and the impact of 'corporate governance'. The concluding section of the paper will highlight the integrative nature of these changes, with reference to the importance of 'board culture' on corporate govern***ing*** and decision making.

* Address for correspondence: School of Management, University of Bath, Bath BA2 7AY. Tel: 01225 826128; Fax: 01225 826473; Email: a.j.pye@bath.ac.uk

Current context

Looking back over the last ten years, much has changed. The late 1980's was an economically buoyant time. Margaret Thatcher had been in power for 10 years and still had another eight to go. Organizations had little difficulty raising money. We had not had the Stock Market crash of 1992, or the Lloyds Underwriters disaster or the Barings Bank or the Long Term Capital Management collapses. From the point of view of corporate governance, Robert Maxwell was still alive and the Cadbury, Greenbury, Hampel and Turnbull committees had not even been dreamt of. Perhaps hardest of all to imagine, PCs were still relatively novel and the Internet was, at very most, confined to a couple of Californian Universities and of no commercial significance. This section considers five particular dimensions which seem to have an important bearing on our endeavour to 'repeat' our study of ten years ago.

(i) Changing nature of organizations and their identities

A quick comparison of FTSE listings of 1989 and 1999 indicates a number of significant changes in the make-up of the corporate world: names such as Guinness and Hawker Siddeley Group are amongst others which have disappeared. In our sample of twelve:

- BTR was taken over by Siebe in 1998 and became Invensys;
- Lucas Industries 'merged' with (although many believed it to be a 'no-premium' takeover by) Varity Inc to become Lucas-Varity in 1996 which was subsequently taken over by TRW Inc in 1999;
- Metal Box split into Carnaud MB and Caradon in 1992 with CMB subsequently being taken over by Crown, Cork and Seal Inc in 1995;
- Hanson demerged into five organizations in 1995–96;
- and TSB merged with Lloyds in 1995 to become Lloyds TSB.

Hence, only seven of the original twelve remain with the same corporate label as they had at the end of the 1980s although closer inspection reveals that the label is not necessarily a good indicator of continuing core identity. For example, ten years ago Glynwed International was routinely described as a 'Midlands metal basher'. Since the mid 1990's, it has gradually divested itself of all metal interests and now is entirely focused on pipe systems and food services. Likewise, Avon Rubber, our original pilot study firm, had grown up over the last 100+ years around the core business of Tyres. In 1997, it disposed of the Tyres business to focus on Industrial Polymers. Hence, although carrying the same name as ten years ago, an organization may be considerably different in constitution and operation. This may in part be accounted for as simply the development of 'strategic focus', something which almost *every* current contributor now talks about although it was never mentioned in our previous study.

(ii) Changing nature of conglomerates

The need for strategic focus is sometimes given as the reason for the demise of the conglomerates during that time. BTR has been taken over by Siebe and Hanson has demerged, while others such as Williams and Tomkins have also significantly reshaped themselves to give greater focus to their activity. Often explained as a result of the investment analysts' need to be able to compare 'similar' organizations in order to evaluate performance, our data support the view that it was also a consequence of the sheer size and complexity. That is, where the typical conglomerate was 'deal-driven' (growth by acquisition), it then got bigger, so deals had to get considerably bigger in order to make a significant difference to the whole, thus reducing the pool of available undervalued, potential acquisitions. This is different to the current mega-mergers taking place between the likes of Smith Kline and Glaxo Wellcome: these are driven out of business synergies, reducing costs and strengthening global presence whereas classically there were no cross-linkages between members of a conglomerate. Hence, managing organic growth in a conglomerate also became more complex as the corporate centre needed an ability to appreciate and evaluate investment decisions across a significant breadth of ever-more complex industries. Ultimately, there came a point where the conglomerates' deal-driven approach no longer generated value and they began to focus.

(iii) Changing nature of economic and financial drivers

One key change at the macro-economic level across the last decade which has particular relevance to our subject is the growth of the 'equity culture'. According to Bogler (2000), even without including data from Nasdaq (ie. the US listing for technology stocks), the ratio between the market capitalisation of New York Stock Exchange listed companies and outstanding publicly held US Treasuries has increased by four to one in the last 5 years in comparison with the preceding 12 years of stability where the ratio remained consistently at 3:2. The case in the UK is quite similar: 'international equity investment now makes up a substantial amount of global capital flows, even before taking account of cross-border mergers and foreign direct investment' (Bogler, 2000) and might help to account for why there appears to be considerably greater pressure than before on share price performance.

Looking at publicly available, widely reported, financial figures also indicates changes which have taken place in terms of the way in which companies are compared and ranked. In 1989, *Business 500* – an endeavour to create a UK equivalent to the *Fortune 500* – produced its annual ranking (based on Extel data) of firms by sales, profits and jobs and added a new column, called return on capital. Now, market capitalisation is usually given as the first figure in any such listing of corporate league tables, as demonstrated in the *FT European 500* Annual League Tables and is frequently referred to in our interviews as a prime indicator of corporate performance.

(iv) 'Consolidation' amongst institutional investors

'Consolidation', aka mergers and acquisitions, has been an important part of corporate life in the last decade. A number of investment organizations have merged or taken each other over, concentrating their influence such that Gaved (1997) estimates UK institutional investors control at least 60% of the equity of UK listed companies. This, in turn, can be extrapolated to identify significant concentration of power and influence in the hands of just a relatively few key fund managers.

In addition, the early 1990's saw the initial development of 'active' as distinct from more traditional passive fund management. Although this is what some argue fund managers *should* be doing if they are to conduct themselves responsibly (Hawley and Williams, 1997, Charkham and Simpson, 1999), it is far from the way in which fund management has been traditionally conducted and has led to some important changes. For instance, a visit to the Hermes Pensions Management website (http://www.hermes.co.uk) reveals a huge amount of information, including its Statement on Corporate Governance and Voting Policy. Such information was not available a decade ago but now leaves little doubt about the stance of this particular 'active' fund management firm.

(v) Changes in Corporate Governance

A number of other events across the last decade have lead to what is often described as the 'corporate governance debate' (Charkham and Simpson, 1999). The death of Sir Robert Maxwell and scandals at BCCI and Polly Peck triggered a series of committees with subsequent recommendations being adopted by the Stock Exchange to ensure transparency and integrity in the governance of corporations: notably, by Cadbury (1992), Greenbury (1995), Hampel (1998) and more recently, Turnbull (1999) committees. The first three led to the *Combined Code of Practice* (1997) – an endeavour to ensure best-governance-practice at board level in plcs, with nominations, remunerations and audit committees being the most obvious outcome. In addition, there have been changes to accounting standards in an attempt to increase the clarity and commonality in accounting practices.[2]

Government too has played its part in consultation with industry over a range of aspects of governance. A panel chaired by Paul Myners of Gartmore plc, was set up specifically 'to suggest practical ways in which the relationship between UK industry and institutional shareholders can be improved as a stimulus for long-term investment and development' (Myners, 1995). Further afield, the OECD has also recently published a detailed report on corporate governance and its effects on firm performance and growth (Maher and Andersson, 1999).

These points outline some of the significant changes to the UK corporate context across the last decade and in effect, sketch out the backdrop against which our sample of firms now operate. The next section looks more closely at some of the changes we have found in our current data of board practice and process.

Corporate Governance: an analysis of 1999 data[3]

In both 1989 and 1999, this study was conceived to be about developing our understanding of how it is that relatively small groups of people (ie. boards) 'run' large organizations. In the meantime, use of the phrase 'corporate governance' has become so common place that it is assumed to have some 'common sense' such that, even without prompting, several interviewees have now described our work as being part of the 'corporate governance debate'. Once labelled in this way, it seems to have a slightly pejorative significance, implying something bureaucratic and 'policing' which is at least one-step removed from the practical realities of corporate life. However, if one looks at the assumptions underpinning much of the academic work in this field, this is perhaps not surprising.

Turnbull (1997) comprehensively answered the question 'what is corporate governance' in a very detailed and heavily referenced paper:

> Corporate governance describes all the influences affecting the institutional processes, including those for appointing the controllers and/or regulators, involved in organizing the production and sale of goods and services. Described in this way, corporate governance includes all types of firms whether or not they are incorporated under civil law. (p.181)

This definition sets a very broad and encompassing overview of the topic while Tricker (1994) concentrates his focus more specifically:

> Corporate governance addresses the issues facing boards of directors, such as the interaction with top management, and relationships with the owners and others interested in the affairs of the company, including creditors, debt financiers, analysts, auditors and corporate regulators. (p.xi)

Whichever approach is adopted, clearly much of the work on corporate governance has emanated from a financial perspective, shaped by notions of regulation and controllership. However, as Turnbull (1997) points out, there are at least three other perspectives on the subject (stewardship, stakeholder and political) which, working from different sets of assumptions, lead to different analyses and conclusions.

This paper does not seek to reiterate these distinctions but instead, articulates a particular path through this maze which seeks to bring together both the people ***and*** the processes involved in 'governing' corporate practice. The emphasis on the adverbial is important: 'governance' has a static, objective quality to it whereas governing emphasises the continuing 'full stream of events' (Barnard, 1938, p.21). Weick (1979) points out that 'organization' is a noun which in essence, does not exist: instead, what is known are the actions and accounts of enacting organizing.

> Whenever people talk about organizations they are tempted to use lots of nouns, but these seem to impose a spurious stability on the settings being described. . . .If students of organization become stingy in their use of nouns, generous in their use of verbs, and extravagant in their use of gerunds, then more attention would be paid to process and we'd learn about how to see it and manage it. (p.44)

To retain an emphasis on what we saw as an active, purposeful and continuous sense of executive process, we wrote up our findings of a decade ago in terms of the doing of manag*ing* (Mangham & Pye, 1991).

The combination of people and processes is a very practical driver: that is, if you talk to executives and non-executives, as we do, their roles are without question built out of an integration of both financial and social dimensions. While this observation is perhaps not very new, the key point here is that rather than adhering to the assumptions of a financial perspective – that rules and incentives can be constructed to align the behaviour of managers (agents) with the desires of principals (owners) (Hawley and Williams, 1997) – financial and social assumptions must be brought together in the light of what actually happens in practice at plc board level. In order to encompass more than simply the regulation and controllership assumptions of governance, an appreciation of multiple perspectives is necessary, hence we are adopting an interpretive approach. (See Mangham and Pye, 1991, for further elaboration.)

How boards work – comparing 1989 and 1999 data

How a board conducts itself and reaches decisions seems central to understanding governance and yet is quite under-researched (Pettigrew and McNulty 1995). We first began our work in the late 1980s and found that it is not easy to gain access to board members in large plcs. Of the twelve companies which contributed to the 1989 project, three have effectively dropped from the sample by 1999[4] through takeover. So the data presented in this paper are drawn from the remaining nine firms which contributed to both the 1989 and 1999 projects, enabling direct comparisons to be made: Avon Rubber, Beazer Group, Coats Viyella, Glynwed International, Hanson, Lloyds TSB, Marks and Spencer, Prudential, and Reckitt and Colman (which became Reckitt Benckiser in late 1999). This section illustrates changes in board structure, composition, tenure, age and gender of directors; the role of NEDs and an illustration of how one board seeks to ensure they are kept up-to-speed on key issues; the frequency of meetings and evaluation of meeting process; the importance of share price performance and relationships with fund managers; and the cross-linkages between board directors and their memberships. It concludes on a paradoxical note that across the decade, the one thing which seems not to have changed is the CEs' perception of themselves as agents of change.

Following Cadbury (1992) and Combined Code of Practice (1997), there have been a number of changes brought about to address issues of corporate governance. All the boards in our sample now have Nominations, Remunerations and Audit Committees, generally staffed by NEDs; their Annual Reports include coverage of what is referred to as Corporate Governance, and now all have split the roles of Chief Executive and Chairman. Marks and Spencer was the last to split these roles after considerable public attention and investor disquiet in 1999. In 1988, three firms had combined Chairman/CE roles of which one was about to separate, and a fourth was shortly to combine the roles. Indeed, in only one case out of the nine had the Chairman been recruited to his post from outside the organization: in the remaining eight cases, the Chairman had spent a long time in the organization and had previously worked at executive level and/or board level, most often as CE.

By 1999, four of the nine boards have 'new' Chairmen (ie. appointed from outside the organization in the last five years), four have 'new-ish' Chairmen (ie. appointed within the last five years but drawn from the NEDs on the board) and one has a Chairman who was previously CE of the organization. This last route to Chairmanship is generally becoming less commonplace, in part because fund management firms are not keen supporters of this kind of Chairman. Hermes Pension Fund Management, for instance, is 'generally opposed to a chief executive becoming chairman in the same company' although will consider the composition and balance of a board as a whole in judging whether or not such a chairman could have 'undue influence on board decisions' (Hermes, 1998).

There are differences in age and tenure of directors across the decade. The average CE in our sample is now 52 years old whereas previously he was around 59. Although the executive population on the whole is about ten years younger than it was a decade ago, the difference is not so clear for NEDs: there is still a predominance of older NEDs who tend to be at least a decade older than their executive counterparts. Figure 1 illustrates the details.

Fewer executives in our sample are long-tenured in the same company and the average 'length of service' tends to be lower than it was ten years ago. In 1989, 85% of the executives had worked for their organization for more than 15 years. Now, the figure is around 30% who have been with their organization for more than 10 years although

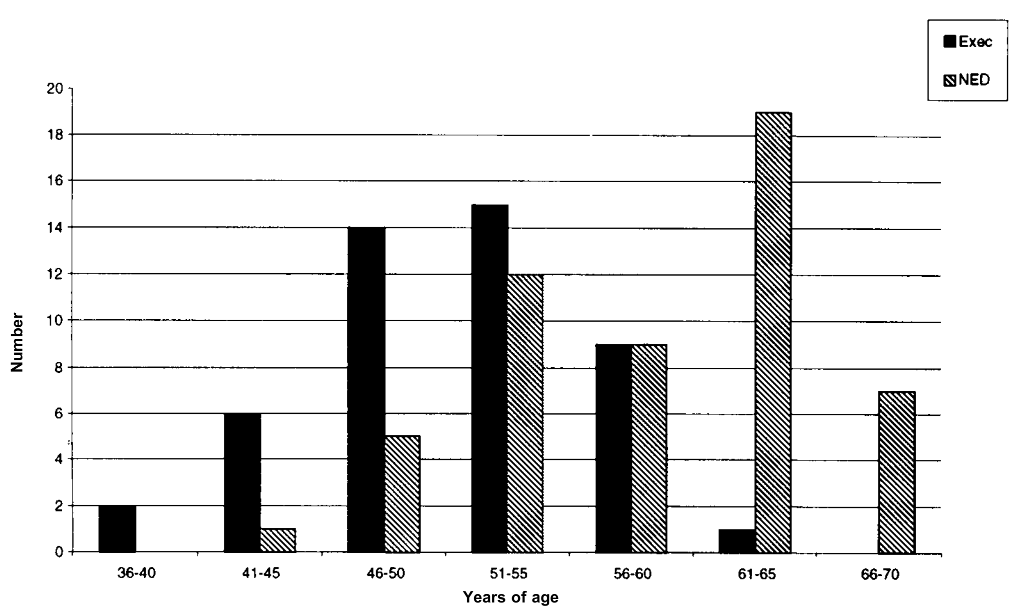

Figure 1. Age of executive and non-executive directors.

none has held their board role for more than nine years. If longer association with an organization inclines towards a more proprietorial view of it, then this attitude is in decline amongst the executive population of our organizations. Turnover is slower amongst non-executive directors: amongst our non-executive sample, ten have held their posts for over ten years.

In the last decade there has also been change to board composition with the percentage of NEDs increasing and each board becoming smaller in total number. For instance, in 1989, TSB board comprised 31 people: 12 Regional Chairmen, 8 executive directors, '8 independents', an executive Chairman and 2 non-executive Deputy Chairmen. This was not uncommon in the banking sector at this time: Barclays and National Westminster both had boards of 28 people, including Regional Chairmen, executives and non-executives.

Well-informed and challenging dialogue was very difficult to achieve in such diffused boards, hence decision making ability and organizational understanding were more circumscribed, such that their function was widely to be seen as 'rubber stamping'. By the late 1990s, most main boards are much more compact (see Figure 2 below) with a balance which in all except two of our sample, reflects more non-executive directors than executive directors and a much greater emphasis on the 'value-added' by members. These findings are similar to those in a survey of FTSE100 boards by Barry (1998). Lloyds TSB remains the largest board in our sample, comprising 7 executive directors and 12 non-executives (including Chairman and Deputy Chairman). The smallest board has 7 members although between 8 and 11 is the most common size.

To some extent, the emphasis on 'value-added' by NEDs has ensured that the number of women NEDs remains as low as it was a decade ago.[5] 'Value-added' is now interpreted to mean that the NED has either previous or current relevant executive experience. Hence, the potential pool from which female NEDs are likely to be drawn is very small indeed. In our sample firms, only two out of forty seven executive directors and five out of fifty three non-executive directors are female. There were no female executives in our 1989 sample: so far, in 1999, there has only been one (out of two) who was available for interview. There were very few female non-executives on any of the boards in 1989 and this continues to be the same in 1999 (see Figure 3).

Some contributors have noted that the significant weight of corporate governance responsibility which has fallen to NEDs tends to cast them in a corporate policing or monitoring role. For instance, the role and title of Senior Non Executive Director has now become an important point of reference for fund management firms. Hermes even offers a six point job description for the Senior NED, proposing that the senior NED should be available to major shareholders for consultation and direct communication and should chair all or most of the subcommittees. Since NEDs mostly comprise the subcommittee membership, it is inevitable that the contribution in terms of time and expertise which is expected of them has changed considerably.[6] Although none of their Annual Reports

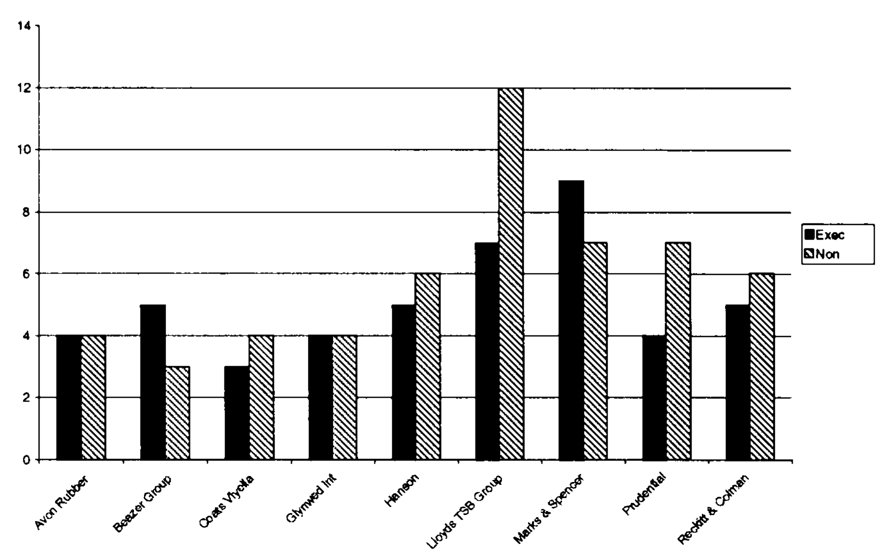

Figure 2. Numbers of executive and non-executive directors in sample companies in 1999.

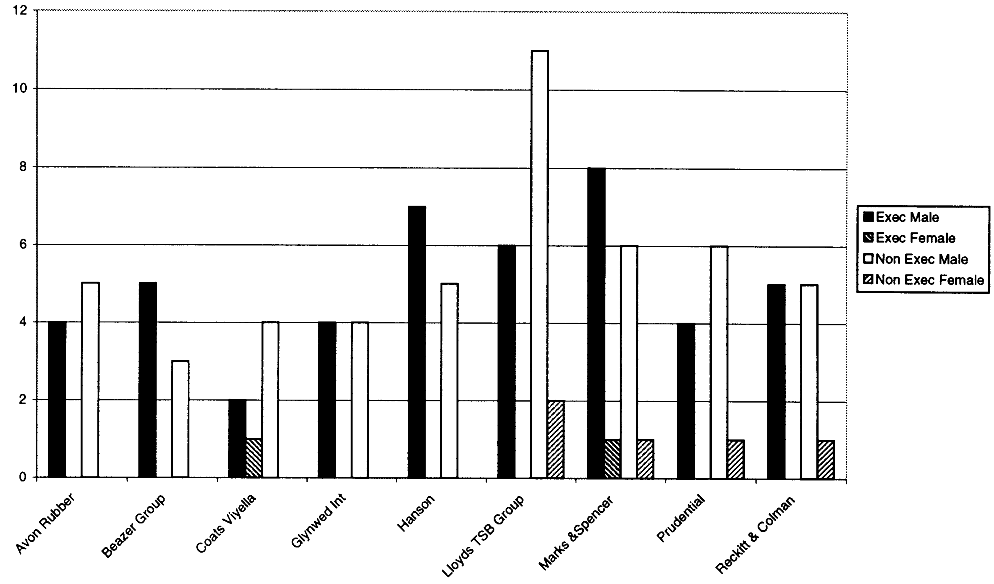

Figure 3. Male/female executive and non-executive directors.

currently note attendance at board meetings, several said they feel this may happen soon, adding to the increasing public awareness of the NED contribution. The only exception to this point is for the NED who is also a practising executive on another board – here, full attendance at each meeting seems to be traded off against 'live' executive expertise. Thus, NEDs now seem to be much more influential in terms of board decision making than was previously the case.

In the past, NEDs tended to be seen as either allies of the Chairman or to have connections in to 'the right networks'. So for example, it was not uncommon to find senior civil servants, Ambassadors or even the wives of politicians on these boards. With one exception, the few who remain on boards in our sample were appointed in the early 1990s and are likely to be retiring over the next few years. In contrast to 1989 practice, it is now much more common place now to use recruitment agencies which concentrate on NED selection.

Yet, for all the formality of drawing up selection criteria and evaluating competence and skill levels prior to appointment, when one asks how the actual NED contribution is evaluated, it seems to be just as much based on 'gut feel', knowing the person and relying on the unspoken rules of 'elite membership' ('we'd soon know if they weren't reading the board papers') as ever before. Given that most admit that it takes at least a year for a NED to learn how a particular organization and board actually work and to have any sense of process or understanding of how to contribute effectively, reliance on peer pressure sounds rather ambiguous. From discussions both with NEDs and Chairmen, it seems that the Chairman plays a significant part in 'conducting' the NED ensemble: bringing forward potential names for consideration, inducting new NEDs and enabling them to contribute.

We have one illustration where the Chairman organizes meetings known as 'the Board-in-Committee' which are 'to discuss a particular topic and to ensure that the Board is sufficiently aware of it'. Unlike an away-day, this meeting usually lasts about two hours, focuses on one subject only (eg. the HR policy of the company, women in the company, credit cards, e-commerce, Latin America etc), and is not a decision-making forum. Instead, it is a meeting at which NEDs are expected to ask questions:

> . . .to enter ''lively debate. . ..to really understand issues. . .there's no covering up of anything at all, whatever it is, what is [our] actual policy on that and how does it work out in practice . . . In our case, the [main] Board Meeting would normally last about three to four hours . . . We get the routine items out of the way as quickly as we possibly can, so the routine items ought not to take more than three quarters of an hour. It's what happened in last month's results, that sort of thing, a few bits and pieces that you pick up from the last month, but you've got now three hours to discuss strategic issues. But when they're looking at these strategic issues, they're some of the big issues and if you were going to teach

> them all about that, to reach a decision, you'd occupy the whole Board meeting.'' (Chairman)

This Board-in-Committee meets about five or six times a year and has an educational purpose, primarily aimed at ensuring that when these important strategic issues are the subject of full board discussion, the NEDs are sufficiently well-informed to fully enact their role.

Other boards have 1 or 2-day annual away-day meetings for strategic review and planning, although these are seen by some only to have value as 'a bonding exercise' amongst the membership. Most boards were doing something similar a decade ago. However, now they are more likely to change the location in which board meetings are held in order to ensure that the NEDs learn about different parts of the organization as well as providing opportunities for NEDs and executives to meet 'off-site', and conveying a symbolic message to the organization that the centre and its parts are interrelated.

Most Chairmen make regular efforts to meet NEDs, usually individually, outside board meetings – perhaps lunch or dinner once or twice a year as well as regular phone calls and/or letters either to tap into particular specialist expertise or to keep them abreast of corporate developments or more often, both. This perhaps idealised-sounding situation is simply a classic illustration of the idea that if you want someone's support, then it is best to keep them informed and 'on-side'.

There is considerable variety amongst our sample in how often each board meets and the nature of its meetings. In three cases, the full board meets only four times a year whereas in others, the board meets upwards of six times a year and in some cases, monthly. (Previously, most boards met four times a year.) Sub-committee meetings go on alongside this formal main board structure to whatever level is required in order to 'tick the boxes' of corporate governance. Although highlighted by Hampel (1998) as a 'best practice', only one board in our sample appears formally to evaluate board process. A questionnaire is sent annually from the Company Secretary to all board members, seeking their perceptions of quality of debate, balance of the agenda, time spent on particular issues, quality of information etc. Apparently, some adjustments have been made to the process and paperwork of meetings as a consequence. Most other Chairmen felt they would have to address this: as one remarked, 'I can see we may have to look at that (board process) at some point in the future.'

Of the 101 directors in the these nine organizations, one NED appears on two boards; of twenty five previous contributors and directors in three other sample organizations, there are at least eleven cases of 'overlap' amongst them and their FTSE 250 board memberships. Hence what might have already seemed like a quite tightly knit network now appears to be even more closely interwoven which has implications for corporate governance and change of practice. These findings are also confirmed by Barry (1998).

Undoubtedly, to some degree, the Combined Code of Practice has resulted in the need to 'tick boxes' although most agree that board practices and process should be transparent to the outside world. However, a company with ticks in all the right boxes may not necessarily also have good financial performance. So although organizations wish to comply with all the various corporate governance rules, for many this is 'an aside' to the more important question of how to improve the performance of the company.

This is where the two themes of strategic focus and shareholder value seem to crystallize around the third common theme of corporate governance. According to Monks and Minow (1996: 171), directors have a duty of loyalty (to the company's shareholders) and duty of care (to exercise due diligence in making decisions). Undoubtedly, the prime measure of corporate performance is in terms of 'shareholder value', a commonly used phrase which has a variety of meanings.[7] Share price performance, the ultimate indicator, is something over which boards have no 'control' but considerable amounts of indirect and direct influence. The ability to present a strong, persuasive case to major shareholders which demonstrates strategic focus and direction with high levels of potential shareholder returns is likely to receive support from investors.

What is perhaps most significantly different to ten years ago is the fact that this information is now considered an absolute right by some fund managers. As the Chief Executive of one fund management firm put it:

> ...we're not trying to run the companies as institutions.... but we have an absolute right to question whether the board's strategy, management or capital structure is right.... They've got to explain their strategy and convince the management of the investment institution that they're the right people with the right strategy as well.

Back in 1989, CEs were beginning to complain about having to spend time 'talking to the City' but their investment of time in this activity has at least doubled since then, with average estimates being around 20–25% of their time devoted in some way to this. Previously, it would not have been considered appropriate to have an open-agenda meeting with a major investor and we were certainly given no illustration of strategic outlines being discussed with investors in advance of board decision making: both these points are now reversed. This is where a number of issues outlined above seem to converge: the increasing power of institutional investors; the 'equity culture'; the importance of market capitalisation and share price as the key performance indicator; and the emphasis on board accountability through transparent corporate governance. Curiously though, it seems that as concerted efforts are made to make governing organizing more open to view, it becomes more obscured as major shareholders exercise their 'absolute right'.

These are some of the main differences currently found in our data spanning the last decade. A final perhaps paradoxical point to add amongst all this change is that CEs, on the whole, do not seem to see their roles as being very different to what they were in the late 1980s. Even then, our CEs described themselves most frequently as 'agents of change' and they continue to do so. The following section will look more closely at how the complementarity of the roles of Chief Executive and Chairman, in our view, challenges the classic adage of 'the Chair's role is to run the board, while the Chief Exec runs the company' to consider more carefully what happens in the relationship *between* the Chairman and CE.

The chairman and chief executive axis

The previous section has outlined some broad categories of observation which appear to have changed across the last ten years. This section looks more specifically at the relationship between Chairman and CE which seems to have a pivotal influence on board practice and process and ultimately, the governing of an organization. Although the way this relationship is played out varies enormously, an important feature of our 1999 data is that in some cases there appears to be a much more inter-dependent, dynamic partnership rather than the more distant(ced) approach which characterised many Chairman-CE dyads of the late 1980's. There have also been other significant changes in terms of who takes up these roles and their power relationships in and around the board which have some bearing on how these roles are conducted.

The Chairman-CE axis is a difficult theme to untangle because with only two exceptions, our sample of nine offer illustrations of positive Chairman-CE relationships and in each of the two exceptions, access has only been gained to one half of the partnership. However, contributors do also draw on their experiences from other boards to give contrasting illustrations. In addition, we have sought to 'test out' our thesis with other well-placed observers who are outside the sample of nine: these include twenty five previous contributors who now have around sixty NED roles between them, five fund managers and someone who holds two FTSE 100 Chairmanships.

The title of Chairman can be quite misleading. Not only might it have a different subtitle (executive, non-executive, part-time) but also what is expected of the occupant is also different. For example, in one case someone was chosen as a FTSE 250 Chairman because he was already a FTSE 100 Chairman elsewhere in a role which took at least three days a week of his time: the recruiting board only wanted a 'hands off' Chairman. However, some non-executive Chairmen, although almost fulltime in their commitment to their firm, are clear that this is not the same as being an executive Chairman: an executive Chairman has a close hands-on involvement and may appear to undermine the authority of the CE unless the CE becomes more of a Chief Operating Officer. Amongst those who describe themselves as non-executive, we find illustrations which range between one who works 4 days a week and another who appears for three consecutive days, once every 6–8 weeks, prior to a board meeting while spending the rest of his time in the US.

The former illustrates what seems to be an exceptionally strong Chairman-CE relationship: in the latter's case, there was only a weak relationship between the Chairman and the CE. Where there is a high level of respect between Chairman and CE and good levels of understanding, rapport and ultimately trust on both sides, then it appears to have a very powerful effect on the board and its decision making. The following lengthy quote, from a Chairman in our sample who also Chairs another FTSE 100 firm and is a NED of another, sums up some of what this means in practice, effectively contemporising the adage:

> And it's absolutely key that the Chief Executive runs the business, *absolutely key*. You mustn't have people second guessing,

> so (CE) and I will frequently have chats ... it's about strategy, it's about fundamental long term things that we want to do, it's about knotty problems ... we're having these discussions the whole time, but (CE) runs this business, not me. There must be no doubt about that ... I'd be the sort of Spanish Inquisitor, if you like.... I mean we could *never* take something like that to the Board if we didn't agree.... This is the key to the Chairman and the Chief Executive that to some extent, the Chairman is a sort of check: I don't mean a check in a way of stopping, but (CE) wouldn't want to take anything to the Board unless I was going to endorse it, and... the last thing I'd want to do is put an idea to the Board if (CE) didn't think it was the right thing to do. But he has to put the thing to the Board and I have to endorse it, it's that way round, it's not me taking the initiative. Of course, the chemistry between two people is *so essential* in this. We say 'how are we going to do this best together'... (emphasis in the original)

NEDs also comment on the influence of Chairman and CE. In one case, two have separately noted that they are 'worked very hard' by the Chairman and the CE but that the collective effort and output is felt to be worthwhile. Notably NEDs also seem to have fun: that is, there is an immense sense of satisfaction, enjoyment and personal development to be gained through this collective effort. Indeed, we have several illustrations of where people have ceased to be NEDs because they found that this sense of satisfaction was no longer being generated.

> ... I think chairmen can be major destroyers or major value adders to the effectiveness of non execs.

> I have resigned from X, there's not a great big mystery about it, but I was feeling that I wasn't really being heard.

From the accounts of board members, much seems to be attributed to the skills, abilities and awareness of the Chairman-Chief Executive axis or synthesis. It is more than just a complementarity of skills: whether the relationship works well or badly, it creates something more than the sum of parts. In the latter case, it creates a hostility and distrust which is greater than either individual could create while in the former, they are seen and trusted to work as a pair which has more impact than either could individually. Although during the course of interviews we have tried to push respondents into articulating their implicit appreciation of the collaborative energy, it seems difficult for the most part for people to identify the essential 'what' which makes a difference, in part because it is different in every case.

> I think their (CEs') effectiveness can be hugely enhanced or hugely destroyed by the chairman ... the chairman's behaviour is going to be coloured by his relationship with the chief executive ... but if the chairman and the chief executive are not getting on very well, the chairman could start to be a bit trivial and start to gang the non execs against (the CE). You know, you can get all sorts of silly board behaviour, silly human behaviour ...and I have seen some bad behaviour between the chairman and the chief exec – fortunately not very often.

From the way contributors talk about their board experiences, it seems that the relationship between Chairman and CE provides an important underpinning to what might be called 'boardroom culture'. If you take the view that culture is something developed by a group of people working together over time as they develop shared ways of doing things (Schein, 1999), then one is just as likely to find a cultural dimension which shapes 'the way things are done around here' in the boardroom as elsewhere. Definitions of culture are usually drawn from notions of values and attitudes (Brown, 1995) and there is undoubtedly an element of common values and shared understanding which underpins strong relationships. From our wider database, we have quite a lot of evidence of the Chairman-CE relationship providing a strong thumbprint on the way things are done by a particular board.

Data from fund managers also describe the particular power evinced by Chairman-CE partnerships which is seen to colour the way in which the whole board works. Hence, there has to be cohesion and coherence in the way the Chairman and CE present themselves outside the organization as well as inside. In one case, a well-known strategic thinker Chair was seen to be the ideal partner for a very sharp, hands-on operator CE in a FTSE 100 turnaround situation. The fact that they have continued to work as a partnership and delivered to the City all that they have promised means that their share price has held up, even during the time when a significant executive was poached away by another firm.

Even fund managers admit to not quite knowing the full details of how a board may work and yet their evaluations of likely future value is based on their judgement of its boards strength. When asked on what is this judgement based, ie. *how do you evaluate a whole board?*, the answer came back:

> Well, ... it is a holistic view of the area. You have a look at the board as a whole and you say, are these people the sort of people who, if there is a problem, would stay, hang tough? ... the chemistry of a board is a very delicate and interesting flower – different in every case.

Inevitably, in the first instance, their view is shaped by the CE and Chairman and only when problems are perceived, would they turn to the senior NED. It is likely that members of the fund management team may know other board members in a particular organization, hence they also develop ways of sharing their knowledge with each other. However, this is still ultimately a human judgement of another human being or beings in which *how* they appear to interrelate or work together can have a very powerful effect.

Conclusions

In the course of interviewing across every category of our contributors, the partnership between Chairman and Chief Executive seems to be the linchpin of the board: effecting how it is put together, how it works and ultimately 'the way things are done around here' rather than just the way things are said to be done around here. Although this assertion cannot be 'measured', our data offer evidence that this is different to what we found a decade ago. Previously, in the six out of nine which had separate Chairmen and CEs, the relationship tended to be very respectful but distant, in which the CE would keep the Chairman informed but remaining primus inter pares: that is, the CE was the fulcrum. Now it seems that the Chairman-CE relationship holds the balance: strong individual influence at either end (or at both ends) is not sufficient to 'run' a large organization. It has to be *combined* influence (perhaps a both/and) model, setting a powerful thumbprint on the way in which the board works. In addition, the Chairman-Chief Executive relationship provides an important axis which not only influences board room conduct but also presents to and persuades the outside world, especially those who judge and criticise performance, such as fund managers, stock brokers' analysts and the financial press.

This is where the multiple themes in this paper seem to come together. That is, corporate governance has been a subject of growing academic interest across the last decade as well as enormous practical significance in the corporate world. For board directors, the financial and the social perspectives come together daily in terms of their roles and conduct. Through macro and micro economic change, share price performance has become a primary indicator of corporate performance, usually underpinned by a presentation of corporate direction in terms of 'strategic focus'. Academically, assumptions of the financial and the social perspectives on research need to come together in appreciating corporate governance in practice. Hence, we argue, the focus should be on 'governing organizing' rather than 'corporate governance': that is, on how organizing is enacted rather than on the implementation of regulatory requirements.

NEDs have a duty of loyalty to shareholders which means their primary objective is to create shareholder value. In so doing, the performance of Chairman and Chief Executive is paramount as they tend to be the conveyors of messages to fund managers[8] but perhaps more importantly, they are also the prime shapers of board room culture in and through which the governing of organizing is enacted. Hence, the issue for code-writers is to find ways to ensure that the values of good governance become positively embedded in business culture. Undoubtedly, the Combined Code (1997) has helped to draw attention to important elements, raising awareness and leading to a more common approach to handling matters of governance in large organizations. To this end, change is taking place although like most attempts to change culture, it is a relatively slow process (*FT*, 1999).

There is still very little research available which offers insight into the practice and process of UK plc boards (McNulty and Pettigrew, 1999) as ironically, given the enormous interest in issues of governance, this remains one of the few areas of corporate life which is not readily available for direct scrutiny. Our work across the last decade offers a rare viewpoint at this level which begins to elaborate some of the significant changes in how small groups of people actually 'run' large organizations.

Acknowledgement

The author would like to thank the editor and anonymous reviewers for their insightful comments which helped to sharpen and strengthen the focus of this paper.

Notes

1. We are grateful to the ESRC for their continued funding this work, under grant numbers WF 2925 0020 (1987–89) and R 000236868 (1998–00).
2. The last ten years has also seen in-depth consultation and reviews by bodies such as the Department of Trade and Industry, the Accounting Standards Association and the Institute of Chartered Accountants of England and Wales amongst others, leading to changes in financial reporting data and moves towards a framework of independent regulation for the accountancy profession.
3. At this stage, data has not be cleared with contributors for direct quotation, hence reference to data in this paper will be made in the general rather than the particular.
4. These are: BTR which merged with Siebe to become Invensys, LucasVarity and Metal Box which both became US-owned, following the takeovers by TRW and Crown Cork and Seal, respectively.
5. The National Management Survey (1998) indicates that the number of women employed at director level actually declined in 1997.
6. A recent report by 3i estimates non-executive directorships in FTSE 100 firms now average around 50 hours per year.
7. One FD defined this as share price appreciation plus dividend, giving total shareholder return. A rather more complex and comprehensive calculation is used in the FT European Performance League Tables (18th June 1999) of total shareholder return as being 'what an investor theoretically receives from a shareholding over a given period, taking into account both the capital appreciation (or fall) in the company's share price, dividends, and any corporate actions over the period, such as new share issues'.
8. Conveying such messages is crucial to the judgements made by fund managers. As one pointed out, financial data is widely and publicly available, hence ultimately the fund manager's differentiating ability depends on her/his judgement. As one put it: '. . . we apply our corporate governance code pragmatically.' '*By which you mean?*' 'Well, we will listen to reason.'

References

3i, (2000) 'Independent Chairmen and non-executive directors survey', *Top Pay Research Group*, London: 3i.

Barnard, C.I. (1938) *The Functions of the Executive*, Boston, MA: Harvard Business School Press.

Barry, R. (1998) The One Thousand: The Men and Women Who Command the Heights of the UK's Economy, Report for The Royal Academy of Engineering and The Engineering Council, published by *The Institute for Employment Research*, University of Warwick, UK.

Bogler, D. (2000) Equity culture becomes the new Pied Piper, *FT*, 21.2.00.

Brown, A. (1995) *Organizational Culture,* London: Pitman.

Cadbury, Sir Adrian (1992) *Report of the Committee on the Financial Aspects of Corporate Governance*, London: Gee & Co Ltd.

Charkham, J. and Simpson, A. (1999) *Fair Shares: The Future of Shareholder Power and Responsibility*, Oxford: Oxford University Press.

Combined Code of Practice (1997), London: Gee & Co Ltd.

Financial Times (1999) 'Most companies flout code on corporate governance', *FT*, 20th Dec, p.18.

Gaved, M. (1997) *Closing the Communications Gap: Disclosure and Institutional Shareholders*, Institute of Chartered Accountants of England and Wales.

Greenbury, Sir Richard (1995) *Directors' Remuneration,* London: Gee & Co Ltd.

Hampel, Sir Ronnie (1998) *Committee on Corporate Governance, Final Report*, London: Gee & Co Ltd.

Hawley, J.P. and Williams, A.T. (1997) The Emergence of Fiduciary Capitalism**,** *Corporate Governance,* 5(4), 206–213.

Hermes (1998) 'Statement on Corporate Governance and Voting Policy', *Hermes Investment Management Ltd,* London.

Maher, M. and Andersson, T. (1999) Corporate Governance: Effects on Firm Performance and Economic Growth, *OECD Secretariat.*

Mangham, I.L. and Pye, A.J. (1991) *The Doing of Managing: A Study in Executive Process*, Oxford: Blackwell.

McNulty, T and Pettigrew, A. (1999) 'Strategists on the Board'. *Organization Studies*, 20:1, 47–74.

Monks, R.A.G. and Minow, N. (1996) *Watching the Watchers*, Oxford: Blackwell.

Myners, P. (1995) *Developing a Winning Partnership*, London: DTI.

National Management Survey (1998), *Institute of Management*, June.

Pettigrew, A. (1995) 'On Studying Managerial Elites' in H Thomas, D O'Neal and J Kelly (eds) *Strategic Renaissance and Business Transformation*, Chichester: Wiley.

Petttigrew, A. and McNulty, T. (1995) 'Power and Influence in and around the Board-room', *Human Relations*, 48:8, 845–873.

Schein, E.H. (1999) *The Corporate Culture Survival Guide*, SF: Jossey Bass.

Strategic Management Journal (1999) 20:11, 1063:1086.

Tricker, B. (1994) *International Corporate Governance*, Englewood Cliffs: Prentice Hall.

Tricker, B. (1999) Editorial: Where do we go from here? *Corporate Governance*, 5,(4), 77–179.

Turnbull, N (1999) 'Corporate Guidance for Internal Control', London: Gee & Co Ltd.

Turnbull, S. (1997) Corporate Governance: Its scope, concerns and theories, *Corporate Governance,* 5(4), 180–205.

Weick, K.E. (1979) *The Social Psychology of Organizing,* NJ: McGraw Hill.