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EVOLUTION OF CORPORATE GOVERNANCE: A Comparative Analysis of the Concept of CEO-Chairman duality in the US, UK, and India

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EVOLUTION OF CORPORATE GOVERNANCE: A Comparative Analysis of the Concept of CEO–Chairman Duality in the US, UK, and INDIA

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[Abstract: *Power struggles have long been a defining feature in the dynamic arena of global corporate affairs. Within the intricate web of corporate structures, clashes often erupt as various factions vie for control. Corporate governance has sought to mediate these conflicts, aiming to rectify the inherent imbalances between management and the company's shareholders or stakeholders. A pivotal mechanism in attaining this balance has been separating the Chairman of the Board and Chief Executive Officer (CEO) positions, a concept traditionally garnered strong backing in nearly all corporate structures worldwide. However, disastrous financial crises across different nations prompted the delineation of these two functions, followed by a growing trend advocating for the division of responsibilities between the CEO and the board's Chairperson. Although numerous companies continue to have a single individual occupying both the roles of CEO and chair, investors regularly voice their apprehensions regarding the potential negative impact of this duality of the CEO-chair position on the board's independence and ability to function effectively. Efforts to address this issue have spanned the globe, with various approaches and degrees of success. This paper embarks on a journey to trace the evolution of corporate governance practices in three influential nations: the United States, the United Kingdom, and India. The objective is to tap into the progress made in these countries and dissect the rationale put forth by regulators worldwide for maintaining a separation between these pivotal positions.*]

I

Introduction

In the ever-shifting realm of global business, a fierce wind of change has swept through, rearranging the corporate chessboard with unprecedented force. This transformative gust bears the name of "corporate governance," a complex dance of interests and objectives, accountability, transparency, and responsibility. It is the

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soul of the corporate world, now at an all-time high attention. The catalyst for this seismic shift can be traced to the brink of disaster that loomed over multiple financial giants. This near-collapse sent shockwaves throughout the global business landscape, and suddenly, the voices from the highest echelons of corporate management grew louder, reverberating across boardrooms and stock exchanges. The call for accountability and transparency resonated with a resounding urgency.

In response, a harmonious effort of nations set out to craft a collective action plan, a symphony of regulations aimed at making corporations accountable to their shareholders and stakeholders. This concerted effort unfolded against a backdrop of power dynamics within the corporate structure, with an individual often perched at its zenith. Regulators and investors alike realized the perils of unchecked power, a realization that rippled through the corridors of power. This outrage by shareholders & investors can also be seen by just observing the change in the board composition over the years of the top S&P 500 companies (As of June 2022, the share of independent board chairs in the S&P 500 surged from 30% in 2018 to 37%, while companies uniting the chair and CEO roles dwindled from 49% to 44%.) listed on the world's largest stock market of the United States.

One of the most contentious issues in corporate governance worldwide lay at the heart of this transformation: Should the CEO simultaneously serve as board chairman? A strategy to separate these positions was proposed in numerous nations, and India, a stalwart in its support of the dual roles, was no exception. The debate raged in India, where 54% of the top 500 listed companies still resisted the voluntary compliance of separating the CEO and Chairperson roles.[1]

Strikingly, the empirical evidence remains elusive despite the global clamour for the separation of CEO and Chairman roles and the backing of shareholders and institutional investors. While influential committee reports like the Kotak and Cadbury reports[2] Advocated for this separation, we need proof that board independence enhances a company's efficiency. Research yields mixed results, with some studies finding no significant correlation between board leadership structure and firm performance.

Amid this inconclusive empirical landscape, shareholder activists and governance experts press on, tirelessly pushing for the division of these roles. The argument is straightforward: Having a company's dual CEO/Chairman situation is akin to marking your exam papers, as the inherent conflicts between the roles demand separation. In a world where shareholder activism takes centre stage, having the

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1 SEBI board meeting, SEBI *available at* https://www.sebi.gov.in/media/press-releases/feb-2022/sebi-board-meeting_56076.html (last visited September 14, 2023).

2 Cadbury Report (the financial aspects of corporate governance) - ECGI, https://www.ecgi.global/code/cadbury-report-financial-aspects-corporate-governance (last visited September 13, 2023).

most potent form of independent board oversight becomes paramount. It's a move that can uplift shareholder morale and bolster trust.

This paper embarks on a journey through the intricacies of this separation, exploring how different nations crafted their laws to mandate the divide between the CEO and Chairman roles. It's a story that unfolds against each nation's unique economic and financial landscapes, a narrative of adaptation and evolution in the ever-evolving symphony of corporate governance.

To delve into the difference of roles of CEO & CHAIRMAN in the governance of a corporate institution, the present work delves into two fundamental objectives- *firstly*, the arguments in favour and against separating the position of CEO and CHAIRMAN, and *secondly*, deciphering the stand taken up in the corporate governance structure of the UK & USA regarding the duality of the CEO/CHAIRMAN.

II

Insights into the Roles of CEO & Chairman in the Governance of the Corporation

A. Delving into the Positioning and Roles of the Chairman & CEO in Governance vis–a–vis Management of the Company

"As the central organ within the modern corporation, the Chairman, in collaboration with the board of directors, bears responsibility for a range of pivotal functions in corporate governance. Firstly, the board actively makes critical business decisions for the corporation, including mergers, matters related to the issuance of stocks, and modifications to the company's governance documents.[3] The board frequently delegates most day-to-day operational decision-making to the management team. Secondly, the board is an invaluable resource for management, providing insight and guidance and facilitating the firm's connections with various resources.[4] Thirdly, the board assumes a monitoring role, holding a fiduciary duty to represent the interests of the corporation's shareholders about the management.[5] However, it should be noted that the specific responsibilities of the chair may vary from company to company; it typically involves acting as a bridge between the board and

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3 See STEPHEN M. BAINBRIDGE, CORPORATE GOVERNANCE AFTER THE FINANCIAL CRISIS, 40 (2012).

4 See *Id*. at 44

5 Michelle M. Harner, Corporate Control and the Need for Meaningful Board Accountability, 94 MINN. L. REV. 541, 583 (2010).

the C-suite, ensuring transparent communication and the smooth flow or exchange of information between these leadership groups.

Beyond these responsibilities, the chair's role extends into the realm of orchestrating board gatherings, crafting the board's strategic itinerary, wielding the power to greenlight or veto financial dealings, offering counsel on policy intricacies, determining the compensation packages of top brass, and guiding the intricate dance of succession planning for leadership. Moreover, the chair frequently acts as the bridge to shareholders when needed. It's worth noting that the chair occupies a commanding position within the board's hallowed chamber, allowing them to shape discussions and influence the direction of crucial votes. Essentially, the chair stands at the board's helm, steering its course through decision-making, advisory duties, and vigilant oversight in formal proceedings and behind-the-scenes interactions.

In corporate governance, board directors bear a sacred trust, with pivotal roles in decision-making, consultation, and vigilant oversight. However, the essence of their role has transformed in recent decades, with the advisory aspect yielding precedence to vigilant monitoring.[6] It has become customary for boards to delegate a significant share of operational authority to the capable hands of corporate officers. As the daily helmsmen, these officers navigate the intricate waters of business. Yet, the board's paramount duty transcends these operational realms. Their true calling is vigilant overseers, ensuring that executives consistently align with the interests of shareholders, not their self-interest.

Similarly, boards of directors stand as stalwart protectors of shareholder interests, akin to the frontline defenders against any spectre of managerial inadequacy. Their mandate is clear: safeguard the shareholders and serve as the first defence against mismanagement. These 180 degrees of turn towards emphasizing the watchdog role of corporate boards have ignited a spirited debate about the board's optimal composition. In today's corporate arena, the presence of directors donned with the badge of "independence," endorsed by both the company and the wider public, stands as an unmistakable standard. Shareholders now elevate the board's prowess, or at least the illusion of it, in the realm of meticulous management scrutiny, placing it above the board's traditional functions of networking, business counsel, and wise insights.

Critics have spotlighted a conspicuous deficiency in corporate boardrooms – their perceived failure to monitor and appraise the CEO's performance vigilantly. Shareholders no longer seek the board as a convivial companion to management but as a sentinel standing sentinel over the company's day-to-day operations. Often grappling with conflicts of interest distinct from those of the shareholders, the board is now summoned to serve as the ultimate defence against management's potential excesses.

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[6] Yaron Nili, Out of Sight, Out of Mind: The Case for Improving Director Independence Disclosure, 43 J. CORP. L. 35, 43-44 (2017)

B. Arguments in Support and Contrast with the Concept of Duality of CEO/Chairmanship Role in a Company

B1. Arguments Supporting Separate Positions

Separating the CEO and chair roles aims to enhance effective management oversight by the board.[7] Combining these roles may lead to excessive power and conflicts of interest between the board and management. This becomes evident when considering their specific responsibilities.[8]

The CEO manages day-to-day operations, while the chair supervises management decisions for shareholders' benefit. Having one person in both roles can create conflicts, particularly in performance evaluation, executive pay, succession planning, and director recruitment. An independent chair is likelier to provide an unbiased management assessment, whereas a CEO chair may tailor information to their interests, potentially harming shareholders. A dual CEO chair is like "grading their exam papers." Furthermore, when a CEO-chair leads a company, the board faces an awkward situation of evaluating their own chair's performance.[9] This scenario may cause directors to avoid their duty of impartially assessing management. Since management's decisions can affect directors' positions and careers, they might hesitate to intervene in the CEO-chair's actions, as the CEO-chair effectively holds a higher rank.[10] This reduced oversight and evaluation could unintentionally empower CEO chairs and lead to excessive compensation.

Apart from reducing agency costs and improving management oversight, separating the CEO and chair roles offers other benefits, such as enhancing board performance and decision-making. Some experts suggest that dividing these roles allows the CEO and chair to focus more effectively on their responsibilities. This separation enables the CEO to concentrate solely on strategy, operations, and organizational matters, while the chair can focus on overseeing management, leading the board, and handling governance-related issues.[11] Additionally, an independent outside chair is introduced as part of this division. In that case, they can bring a fresh and unique perspective to the board, facilitating swift improvements in the company's operations and decision-making processes.

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[7] Independent Board Leadership, COUNCIL OF INSTITUTIONAL INV., https://perma.cc/8J6Q-NUY8 (last visited September 23, 2023).

[8] David F. Larcker & Brian Tayan, Chairman and CEO: The Controversy Over Board Leadership Structure, STAN. CLOSER LOOK SERIES, 1, (2016)

[9] Thuy-Nga T. Vo, To Be or Not to Be Both CEO and Board Chair, 76 BROOK. L. REV., 88 (2010)

[10] *Id*. 88 – 90

[11] Larcker & Tayan, *Supra note* 8, at 1.

B2. Arguments Supporting Combined Positions

The division of roles has potential drawbacks, primarily concerning its impact on the board's management functions rather than its monitoring role. Opponents of role separation argue that combining the CEO and chair positions strengthens the board's management capabilities by reducing information-related costs, promoting unified leadership, and ensuring consistency in CEO succession. Critics of separation argue that it can increase information costs. They suggest that having a chair with the CEO's strategic expertise and deep knowledge of the company's operations and finances benefits the organization. This CEO-chair can lead the board in understanding and making critical business decisions. Combining the roles also maintains a "unity of command," providing apparent authority for effective leadership, which is crucial for organizational stability and accountability.

Another concern is the CEO succession process. Many US companies follow a "pass the baton" succession approach, where the outgoing CEO temporarily becomes the board chair to facilitate a smooth transition for the new CEO. Permanent role separation could disrupt this process and add transition costs. Whether these costs outweigh the benefits of separation depends on specific circumstances.

III

Corporate Governance in United Kingdom

A. CEOs and Chairmen aren't BFFs Anymore—Time-travel Adventure through the Evolution of UK Corporate Governance Structures

The necessity for a robust corporate governance framework has been acknowledged globally, and the United Kingdom is no exception. In the 1980s, certain UK companies experienced corporate governance failures, exemplified by cases like Maxwell Communications and Polly Peck.[12], characterized by ineffective board performance. Responding to these failures, the

Cadbury Committee[13] The UK took action in 1992 by introducing the Code, known for its best practices. Since then, various enhancements have contributed to fortifying corporate supervision/governance in the UK Subsequent updates to the

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[12] Mallin, C.A., & Farag, H. Balancing the Board: Directors' Skills and Diversity. Institute of Chartered Accountants in Scotland (2017).

[13] Sir Adrian Cadbury Committee, Report of the Committee on the Financial Aspects of Corporate Governance, December 1, 1992, *available at* https://www.ecgi.global/sites/default/files/codes/documents/cadbury.pdf (Last visited on September 10, 2023)

UK codes were prompted by global business failures and financial scandals to prevent situations where an individual within a company holds unchecked power to manage and make decisions for the organization. The Cadbury committee's report was commissioned following significant corporate scandals, including the downfall of the Bank of Credit and Commerce International ('BCCI'), Polly Peck, Coloroll, and Maxwell Publishing.

Over time, the corporate governance framework in the United Kingdom has been widely regarded as an exceptionally effective model, serving as a prominent benchmark for many other jurisdictions in Europe and Asia. This system particularly appeals to international companies seeking access to a diverse pool of investors. These investors are reassured by the stringent governance standards applied to issuers, regardless of where their primary business operations are located.

The United Kingdom's corporate governance system unfolds as a rich tapestry, weaving together an intricate blend of laws, codes of conduct, and market norms. Its authority is derived from a harmonious symphony of obligatory and customary rules, deeply rooted legal principles from centuries of common law tradition, and legislative acts like the Companies Act 2006. Regulatory frameworks, including the Listing Rules and the Disclosure and Transparency, The Financial Conduct Authority (FCA), a venerable statutory guardian, sculpts and enforces rules.

While some of these regulatory threads trace their lineage to European law, others are finely tailored to the unique contours of the United Kingdom's governance landscape. In corporate control, the City Code on Takeovers and Mergers, known as "the Takeover Code," is a formidable sentinel endowed with legal stature.

But the beating heart of this governance mosaic is the UK Corporate Governance Code, affectionately referred to as "the Code." This pivotal Code of Conduct, a creation of the venerable Financial Reporting Council (FRC), itself a guardian enshrined in statute, is periodically crafted and refined. It serves as the guiding star, illuminating the path of corporate governance within the United Kingdom.

In the United Kingdom, large corporations generally adhere to separating roles as part of best practice requirements and after considering commercial needs. A combined chair and executive role is rare in the UK corporate landscape. The division of roles has resulted from the much-awaited oppression from investors, especially institutional investors, to ma, maintain this distinction, and that should be accompanied by voluntary guidelines outlined in the Combined Code.

B. UK's Code of "Comply or Explain"—A Distinctive One

Despite these clear recommendations favouring the separation of roles, the Combined Code has granted companies significant flexibility. The Combined Code is structured into three levels: primary principles, supporting principles, and code provisions. The first two components have been integrated into the London Stock Exchange listing rules, making them obligatory for all listed companies. The code requirements, however, work on the "comply or explain" tenet, enabling a corporation to deviate from them as long as it notifies its shareholders beforehand. In such cases, the corporation must explain its justifications to the shareholders, who then vote in favour of or against the decision via a resolution. The obligatory guidelines in the Listing Rules and the code requirements address this discrepancy between the two responsibilities.

After examining the regulatory requirements and the leeway afforded concerning the separation of CEO and Chairman roles, it is crucial to explore the factors motivating investors to advocate for this division. Investors are driven by the desire for their companies to thrive, ultimately increasing their returns. This motivation shapes their engagement with the board and underscores the significance of transparency and accountability. Consequently, the first rationale behind investor pressure is their belief that companies exhibit more excellent stability and face fewer long-term risks when they resist consolidating power in a single CEO/Chairman.

Secondly, institutional investors in the UK, in particular, are increasingly of the opinion that the Chairman's role should be held by a non-executive director, underscoring the need for a clear separation between these two functions. It's worth noting that some European countries, like Germany and the Netherlands, adhere to a 'two-tier board' structure mandated by law, necessitating the division of CEO/Chairman roles by establishing two distinct boards. In this system, the supervisory board, chaired by non-executive members, oversees corporate governance, while the CEO or its equivalent leads the management board. However, this two-tier structure is not legally enforced in the UK, rendering such compliance mechanisms nonbinding by law. Consequently, most UK firms adopt a unitary board structure in which executive and non-executive directors serve on the same board.

C. The Trail of Historical Evolution of Separating the Roles of CEO and Chairman in UK

The formation of joint-stock businesses in the 17th century may be linked to the historical development of the separation of the CEO and Chairman responsibilities in the United Kingdom. These early businesses had a lot of issues with accountability, agency issues, and conflicts of interest. A distinct separation of duties between shareholders and management was required to overcome these problems.[14] Companies became more extensive and complicated as capitalism

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[14] M. Van Essen *et al*, *Assessing Managerial Power Theory: A Meta-Analytic Approach to Understanding the Determinants of CEO Compensation*, 41(1) JOURNAL OF MANAGEMENT 164-202 (2015).

evolved throughout the Industrial Revolution. As a result, the focus on separating ownership and control increased as shareholders sought ways to guarantee that their interests were safeguarded. As a representation of shareholders' interests, the Chairman—often a non-executive person—emerged, while the CEO assumed control of the day-to-day management of the business.[15] The historical precedent of this dual leadership structure laid the foundation for the modern practice of separating the roles of CEO and Chairman. Over time, this separation became more pronounced, with the Chairman counterbalancing the CEO's operational authority.

For a better understanding of the reasons as to why the United Kingdom follows the separate person rule, we would like to narrate the advantages of the same whimsically. As we embark through the annals and laws governing the UK corporate governance structures, we unravel the intriguing reasons behind the estrangement of CEOs and Chairmen. This investigation reveals five compelling narratives that have reshaped the corporate landscape:

Enhanced Board Independence: We encounter the first chapter—enhanced board independence. For Instance, Picture an independent Chairman as the guardian of shareholder interests, wielding a critical perspective that ensures board decisions are untainted by the operational concerns of the CEO. In this narrative, the Chairman's role transcends mere oversight, becoming a stalwart defender of shareholders' best interests.

Checks and Balances: The next chapter transforms the landscape into a system of checks and balances. Here, the Chairman's role evolves to include overseeing the CEO's performance, ensuring accountability, and averting the perils of power concentration. This narrative paints a vivid picture of harmony within the board, where the Chairman's allegiance to shareholders counterbalances the CEO's operational prowess.

Transparency and Investor Confidence: Our journey throughout the research uncovers another facet—transparency and investor confidence. Imagine investors from diverse backgrounds seeking assurance in a global marketplace. Here, the independent Chairman emerges as a beacon of transparency, instilling confidence in shareholders' hearts. In this narrative, the Chairman becomes the guardian of investors' interests, fostering trust in the organization.

Mitigation of Potential Conflicts: As we venture further, we encounter the narrative of conflict mitigation. The separation of CEO and Chairman roles protects against potential conflicts of interest. The Chairman's independence ensures that decisions

[15] Minichilli, A., Brogi, M., & Calabrò, A. Weathering the Storm: Family Ownership, Governance, and Performance through the Financial and Economic Crisis. Corporate Governance: An International Review, 24(6), 552-568 (2015).

resonate with the company's and its shareholders' broader interests. In this narrative, the Chairman's impartiality safeguards the integrity of corporate decisions.

Effective Leadership Structure

The establishment of an effective leadership structure marks a critical juncture in the dynamics of organizations, particularly evident in the distinct separation of roles between the CEO and Chairman. This differentiation goes beyond mere procedural adjustment; it signifies a strategic evolution aimed at optimizing both corporate governance and operational efficiency.

At the heart of this restructuring lies a fundamental acknowledgment of the divergent responsibilities inherent in executive leadership. By relieving the CEO of governance concerns, the organization enables them to focus solely on navigating the intricacies of day-to-day operations with agility and precision. This undivided attention not only enhances decision-making but also fosters a culture of innovation and facilitates the execution of strategic initiatives, ultimately enhancing overall operational performance.

Concurrently, the Chairman assumes a broader mandate encompassing governance oversight, strategy development, and shareholder advocacy. Positioned at the apex of the corporate hierarchy, the Chairman wields influence not only within the boardroom but also in shaping the organization's long-term vision and external relationships. This expanded role empowers the Chairman to navigate the company through strategic challenges, foster trust among stakeholders, and champion the interests of shareholders with unwavering commitment.

The symbiotic relationship between the CEO and Chairman within this redefined framework fosters a harmonious equilibrium conducive to organizational success. By leveraging their respective strengths and areas of expertise, both leaders collaborate towards a shared goal, thereby maximizing the organization's potential for sustained growth and resilience.

Furthermore, the strategic separation of roles in corporate leadership is not a novel concept but rather a reflection of historical lessons and evolving best practices. Through an examination of the narratives surrounding this structural transformation, we discern a legacy of experimentation and adaptation. The division of CEO and Chairman roles emerges as a pragmatic response to the imperatives of effective governance and leadership stewardship.

Indeed, the echoes of this historical evolution reverberate in the contemporary corporate governance landscape, exerting a profound influence on organizational structures and decision-making processes. As businesses navigate an increasingly complex and dynamic environment, the separation of CEO and Chairman roles underscores the enduring importance of strategic foresight and adaptive leadership in shaping the trajectory of corporate success.

Market Capitalization and Ownership Structure

Separation patterns often differ between large-cap and small-cap companies. Large-cap firms may prioritize separation due to their complex structures and diverse shareholder base, while small-cap may opt for combined roles for simplicity. Market forces profoundly influence the adoption and performance of the CEOChairman separation model within the United Kingdom. This relationship between corporate governance practices and market dynamics is intricate, marked by moments of alignment and divergence.[16]

Investor Activism and Shareholder Demands

The rise of activist investors has pressured companies to adopt governance practices aligned with shareholder interests, potentially driving separation. Shareholders increasingly demand transparency and accountability, favouring separation to achieve these goals.

Market Volatility and Economic Conditions

The popularity of the separation model can fluctuate with economic conditions. During economic downturns, cost-saving measures may lead to role consolidation, while growth periods may encourage independence. Heightened market volatility can underscore the need for effective governance, prompting companies to consider role separation.

IV

Deciphering the Position of Statutory Mandate in the United States

A perpetual tug-of-war unfolds in the vast landscape of American corporate models, where managerial influence reigns supreme. On one side, the allure of a well-established ownership structure beckons, while on the other, the shadow of safeguarding investor and shareholder interests looms ominously. A problem emerges within this intricate tapestry of ownership dispersion—a battle of interests between management and shareholders.

In this complex web, investors who diversify their holdings often find themselves bereft of the zeal to actively police management or allocate resources for such vigilant oversight. This void in watchful guardianship paves the way for managers

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16 Nordberg, D. and McNulty, T. Creating Better Boards through Codification: Possibilities and Limitations in U.K. Corporate Governance, 1992–2010. Business History, 55(3), 348-374 (2013).

to advance their agendas, occasionally at the expense of those they are meant to serve—the shareholders.

However, the chronicles of recent years reveal two pivotal shifts that have acted as a balm to soothe the frictions of this conflict. First, a groundswell of active and passive shareholders has arisen, resolute in their determination to hold corporations and their stewards accountable for their deeds. Second, the spotlight has shifted onto corporate boards, cast now as the primary sentinels guarding the sacred interests of shareholders.

This accentuation of board independence manifests in diverse ways. It includes the emergence of new federal statutes born from the Sarbanes-Oxley and Dodd-Frank Acts, a surge in scrutiny from discerning investors and erudite scholars focusing keenly on board independence.[17] Moreover, with their venerable jurisprudence, Delaware courts have increasingly relied upon independent directors' imprimatur in addressing this perturbing concern, particularly in matters of conflicted transactions.

A. Tracing the Trail of the Evolution of Statutory Mandates in the United States

In the US, the question of splitting the CEO and Chairman roles has emerged due to a complex interplay of factors, including a challenging economic climate, heightened regulatory measures, and growing dissatisfaction among investors. During the early 2000s, stock markets experienced a severe crash that resulted in steep declines in stock prices and big scandals involving the manipulation of stock values and deceptive trading practices. Companies like Enron and WorldCom, initially enjoying soaring stock prices, subsequently went bankrupt, revealing significant accounting/auditing frauds and manipulations that, in the past, had inflated their values artificially. Other companies, such as Tyco and Adelphia, were discovered to be weaker, especially financially, than previously believed, mainly due to executives engaging in extensive self-dealing transactions and personal enrichment.[18]

Severe issues with conflicts of interest between auditors and securities analysts, as well as the lack of proper monitoring to protect auditor independence, were brought to light by these events. It became clear that poor corporate governance procedures

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[17] See Commonsense Principles 2.0, GOVERNANCE PRINCIPLES, https://www.governanceprinciples.org/wp-content/uploads/2018/10/CommonsensePrinciples2.0.pdf (Last visited on September 13, 2023)

[18] Robert Charles Clark, Corporate Governance Changes in the Wake of the Sarbanes-Oxley Act: A Morality Tale for Policymakers Too 1, September 2005, *available at* http://www.law.harvard.edu/programs/olin_center/papers/pdf/Clark_525.pdf (Last visited on September 13, 2023)

and insufficient transparency rules significantly influenced these failures. There is no way to ignore the urgent need for significant changes in light of these appalling examples of wrongdoing that caused widespread anxiety. In light of these changes, shareholders and corporate directors started to doubt a single leader's ability to successfully oversee the day-to-day operations and the governance of an organization, regardless of their competence or talent.

This gave rise to a growing debate about the potential benefits of separating the roles of CEO and Chairman as the necessity for such separation became increasingly apparent. Whether such a division could benefit a company and its stakeholders gained momentum and remains a central topic in discussions on corporate governance in the United States. The US government took bold action in the face of these trials, crafting precise mandates to rekindle public trust. They aim to elevate financial reporting's credibility, refine audit quality, and foster self-regulation via independent committees, all while enforcing harsher penalties for transgressions. This symphony of governance breathed life into a landscape tainted by doubt and uncertainty.

B. Statutory Analysis

The "Sarbanes-Oxley Act of 2002" and the "Dodd-Frank Act of 2010" emphasized establishing a corporate board with a significant share of independent directors. They also underscored the importance of having essential board committees responsible for overseeing audits, executive compensation, and the selection of new independent directors dedicated to implementing reforms. These measures advocate for sound corporate governance practices and result from accumulated policy stances informed by practical exposure and broader policy-based arguments.

I. The Sarbanes-Oxley Act, 2002[19]

This Act of 2002, often called SOX, was a response to corporate scandals marked by major bankruptcies, questionable accounting practices, and neglect by audit firms. SOX's primary goal was to enhance the accuracy and reliability of corporate disclosures required by securities laws to protect investors.

Title III, named Corporate Responsibility, outlined provisions to strengthen corporate governance, requiring specific actions from companies and their management while specifying prohibited activities. Title II, focusing on Audit-Related Changes, mandated that the audit committee be comprised entirely of external board members. This ensured that no company management member responsible for achieving company goals could be on the audit committee responsible for overseeing essential processes like financial reporting for effective corporate governance.

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[19] The Sarbanes-Oxley Act of 2002

However, because committees are typically chosen from the board of directors, the audit committee acts as a subset of the board, reporting to the Chairperson. Having the CEO as the Chairperson could hinder the committee's effectiveness and potentially create conflicts of interest. This concern is amplified when considering §1514A[20]The whistleblower provision of SOX mandates the audit committee to establish a mechanism for reporting fraud and misconduct directly to them without fear of retaliation. Employees may hesitate to say issues now if the board predominantly comprises management. Moreover, the audit committee might not take decisive action on such reports if the CEO simultaneously serves as its Chairperson. Therefore, for the committee to function effectively, it should maintain maximum independence from management.

SOX aimed to address corporate governance problems but faced challenges and criticism, notably after the 2008 collapse of Lehman Brothers during the financial crisis. This event underscored the Act's limitations in effectively tackling all corporate governance-related issues.[21]

II. The Dodd-Frank Wall Street Reform and Consumer Protection Act, 2010[22]

In July 2010, Dodd-Frank revamped SOX, a game-changer in financial regulation. It beefed up whistleblower safeguards, impacting public and private firms alike. Unlike SOX, it doesn't demand CEO-chair separation but asks for a rationale for uniting or dividing these roles.[23]

Post-Dodd-Frank, the SEC tweaked Regulation S-K, part of the '93 Securities Act, setting public firms' disclosure rules. It details how companies decide their board structure. If one person holds CEO and Chairman roles, the disclosure must include whether there's a lead independent director and why they're there.

C. The Emerging Concept of Independent Directors in the United State's Corporate Organizational Structure

To bolster board independence, some companies have embraced appointing a lead independent director alongside a CEO who also assumes the Chairperson's role, striking a harmonious balance. This approach gains traction, partly influenced by a

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[20] The Sarbanes-Oxley Act of 2002, §1514A

[21] See Rosalind Z. Wiggins, Thomas Piontek, Andrew Metrick, *The Lehman Brothers Bankruptcy: An Overview* Volume 1 Issue 1 JOURNAL OF FINANCIAL CRISES 39-62 (2019) *available at* https://elischolar.library.yale.edu/cgi/viewcontent.cgi?article=1000&context=journal-of-financial-crises (Last visited on September 13, 2023).

[22] THE DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT, 2010

[23] The Dodd-Frank Wall Street Reform and Consumer Protection Act, 2010, §972

New York Stock Exchange mandate for executive sessions sans managerial presence, supervised by a "presiding" director.

The lead independent director's role has blossomed in influence, with more firms adopting and fine-tuning its responsibilities. Proxy advisor Glass Lewis observed dwindling support for separate chair proposals, a trend seemingly propelled by the ascendancy of lead independent directors.[24] In 2017, only 11% of S&P 1500 companies lacked either a lead independent director or an independent chair, a remarkable improvement from 2009 when 33% lacked either.[25] Furthermore, 54% of these companies favoured a lead independent director over a 35% preference for an independent chair.[26] Among S&P 500 firms, the scales tipped towards lead independent directors, with 59% reporting their presence in 2018.[27] As of June 2022, the share of independent board chairs in the S&P 500 surged from 30% in 2018 to 37%, while companies uniting the chair and CEO roles dwindled from 49% to 44%.[28]

The lead independent director's core functions include serving as an additional channel for shareholders with limited access to the board chair. They facilitate communication among board members, adeptly mediate conflicts, and significantly counterbalance the board chair's influence, akin to the chair's oversight of the CEO, particularly vital when the CEO and chair share close ties. Additionally, the lead independent director spearheads the assessment of the chair's performance and, when necessary, spearheads the quest for a new chairperson.

While specific duties may vary, the lead independent director embodies an independent leader for the board, offering a viable alternative to splitting the chairperson and CEO roles. This role is a strategic tool for addressing activist investors and sidestepping shareholder votes on CEO-chair separation proposals.

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[24] Amy Lee Rosen, Support for Independent Chairmen Waning, Proxy Firm Finds, CQ ROLL CALL WASH. CORP. GOVERNANCE BRIEFING, WL 3382203, (2016)

[25] KOSMAS PAPADOPOULOS ET AL., INSTITUTIONAL S'HOLDER SERVS., U.S. BOARD STUDY: BOARD ACCOUNTABILITY PRACTICES REVIEW 11, Pg 10 (2018)

[26] *Id*. at 10-11.

[27] Steve Klemash, Jamie C. Smith & Kellie C. Huennekens, EY Ctr. for Bd. Matters, Today's Independent Board Leadership Landscape, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (2018)

[28] To Accommodate Growing Workloads, Boards are Electing Independent Board Chairs, Experimenting with Committee Structures, and Holding More Meetings, The Conference Board, https://www.conferenceboard.org/press/boards-are-electing-independent-board-chairs (last visited September 14, 2023).

V

Mapping One of the Prominent and Substantial Corporate Debates in India: The CEO and Chairman Divide

There is a growing demand for enhanced supervision of the top leadership within companies. This need for improved governance is not only apparent on a global scale but is also gaining momentum in India. Historically, the Indian corporate sector strongly favoured combining the roles of CEO and Chairman of the board. Given that many Indian companies have a concentrated ownership structure, often with family members holding significant shares, there is comparatively less opportunity for shareholder activism in India than in countries like the US or the UK As a result, the likelihood of a company voluntarily adopting separate CEO and Chairman roles is limited when such activism is absent. Recognizing India's reputation for informal corporate practices, Indian policymakers believed a more structured approach to corporate governance was necessary.

A. Going Down the Memory Lane

For more than five decades, the Companies Act of 1956[29], referred to as the 'old Companies Act,' did not explicitly address the separation of the Chairman and CEO roles. The provisions related to appointing managers or whole-time directors primarily focused on the interests of peripheral stakeholders. Section 269[30] The old Companies Act regulated the appointment process for directors and managers, with minimal mention of the differentiation between board and CEO responsibilities. This omission regarding role segregation may have been because it was assumed that a strong board would effectively represent stakeholders' interests. However, this oversight should have addressed the crucial CEO responsibility of ensuring a company's profitability. At the time, legislative drafters likely did not consider this aspect due to the distinctive nature of the Indian corporate structure.

In the latter part of the 2000s, the corporate regulatory framework underwent significant restructuring in response to changes brought about by a liberalized economy. Prominent industrial groups and the Securities and Exchange Board of India (SEBI) played a central role in advocating these changes. SEBI introduced Clause 49 of the Listing Agreement[31], which served as the foundation for transforming

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[29] The Companies Act, 1956

[30] The Company Act of 1956, Section 269.

[31] Securities Exchange Board of India (Listing Agreement to the Indian Stock Exchanges), Clause 49; Afra Afsharipour, Director Notes: A Brief Overview of Corporate Governance Reforms in India, December 2010, *available at* https://papers.ssrn.com/sol3/Delivery.cfm/SSRN_ID1823563_code366600.pdf?abstractid=1729422&mirid=1&type=2 (Last visited on September 10, 2023)

corporate boards in India, leading to increased transparency and disclosure for stakeholders. SEBI's efforts continued with the establishment of the Birla Committee in 1999[32], which recommended measures to enhance corporate governance for listed companies. These measures included the establishment of audit committees to bridge the gap between shareholders and management. These recommendations were subsequently incorporated into later amendments to Clause 49.

Amid concerns about instability in the American markets, SEBI formed the Murthy Committee to address issues related to the structure and independence of corporate boards and insider trading. Two other committees also examined director independence and auditing reforms.

Collectively, these committees reshaped India's corporate governance landscape.

Following the Satyam scandal, the Confederation of Indian Industries (CII) conducted an extensive analysis, and various industrial groups established committees to assess the scandal's impact. While the CII took a defensive stance, characterizing the scandal as an 'isolated incident,' the Indian government initiated inquiries by SEBI and the Ministry of Corporate Affairs (MCA). Interim measures were implemented, including appointing government-nominated directors, and SEBI and MCA introduced remedial measures, including amendments to the Listing Agreement and the Corporate Governance Voluntary Guidelines (2009). However, it's worth noting that the latter remained in the realm of recommendations, underscoring the need for more binding guidelines.

B. Delving into the Present Stand taken by SEBI

In a decisive board meeting on February 15, 2022[33], SEBI shook things up, granting the top 500 listed companies the autonomy to decide whether they want to keep the positions of Board Chair and CEO intertwined or separate. This was a notable shift from their earlier stance, established in 2018 when SEBI amended the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015[34], making it a

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32 Shri Kumar Mangalam Birla Committee, Report of the Kumar Mangalam Birla Committee on Corporate Governance, 1999, *available at* https://www.sebi.gov.in/sebi_data/commondocs/corpgov1_p.pdf (Last visited September 9, 2014).

33 SEBI board meeting, SEBI, https://www.sebi.gov.in/media/press-releases/feb-2022/sebi-board-meeting_56076.html (last visited September 14, 2023).

34 Securities and Exchange Board of India (listing obligations and Disclosure Requirements) Regulations, 2015 [last amended on January 24, 2022], SEBI, https://www.sebi.gov.in/legal/regulations/jan-2022/securities-and-exchange-board-of-india-listing-obligations-and-disclosure-requirements-regulations-2015-last-amended-on-january-24-2022-_55993.html (last visited September 14, 2023).

requirement for the top 500 entities to ensure that the Chairperson was an unrelated non-executive director distinct from the Managing Director or CEO.

Initially slated for enforcement on April 1, 2020, the deadline was pushed to April 1, 2022, after industry voices expressed concerns. The initial push to segregate the Chairperson and CEO roles stemmed from the 2017 Committee on Corporate Governance report, commonly known as the Kotak Committee.[35] This recommendation aimed to strengthen board independence and reduce concentrated power. With a growing emphasis on the board's watchdog role, concerns surfaced about potential conflicts of interest if a single individual assumed both positions. The Companies Act, 2013, in Section 203[36], explicitly prohibits the simultaneous occupation of the Chairperson and CEO roles, except when a company's articles of association allow it.

However, SEBI's decision to pivot toward voluntariness came after facing resistance from the industry and witnessing only a slight uptick in compliance rates, from 50.4% to 54.0% between September 2019 and December 2021.[37] Some contend that existing Indian corporate laws already encompass sufficient measures to address conflicts of interest. These include requirements for independent directors and limitations on voting by interested parties in related-party transactions. Given India's regulatory tradition, which historically leaned toward stringent corporate governance rules rather than flexible, soft-law approaches like the UK, SEBI's shift toward voluntary separation is a noteworthy departure. It aligns with the principle of shareholder democracy stipulated in Section 203, allowing each company's shareholders to decide whether they prefer a unified or separate Chairperson and CEO structure.

However, it's worth noting that voluntary governance measures have had limited success in India, unlike in some other jurisdictions.

C. Showing the True Essence of CEO–Chairman Power Separation: the Cadbury Committee Report

When it comes to defining the roles and responsibilities of a Chairperson, the Companies Act 2013 needs more clarity. In such instances, we refer to the Cadbury Report.[38], which has established a global standard for corporate governance. The

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35 Report of the Committee on Corporate Governance, SEBI, https://www.sebi.gov.in/reports/reports/oct-2017/report-of-the-committee-on-corporate-governance_36177.html (last visited September 14, 2023).

36 The Company Act 2013, Section 203.

37 SEBI board meeting, SEBI, https://www.sebi.gov.in/media/press-releases/feb-2022/sebi-board-meeting_56076.html (last visited September 14, 2023).

38 Cadbury Report (the financial aspects of corporate governance) - ECGI, https://www.ecgi.global/code/cadbury-report-financial-aspects-corporate-governance (last visited September 13, 2023).

report's analysis underscores the significance of separating the roles of a CEO and Chairman to enhance oversight. The Cadbury Report states that the CEO is responsible for overseeing all executive operations of the business, including the execution of corporate strategy, evaluation of operational activities, and overall business performance. In contrast, a neutral party in charge of rating the CEO and the rest of the management team should hold the post of Chairperson.

It was clear that the appraisal process may be biased if the same individual, or someone closely related to the CEO, held both posts. As it would insufficiently reflect the stakeholders' interests, this might jeopardize the whole evaluation process. As a result, it was suggested that different people hold the CEO and Chairman positions.

It became clear that the CEO and Chairman jobs needed to be separated since many Indian businesses are family-owned and -operated. This division guaranteed the safeguarding of shareholder interests and avoided the consolidation of power in the hands of one person. The

Cadbury Report's recommendations provide insightful information on the value of job separation in fostering accountability and openness in corporate governance.

D. Some of the Impediments to the Successful Implementation of the CEO–Chairman Post Separation in India

The lack of convincing data demonstrating that an independent chairman substantially impacts a company's performance or governance quality led SEBI to decide against a rigid requirement for CEO and Chairman separation.[39] However, SEBI's insistence on the independence of the Chairperson from the CEO presented challenges for succession plans, particularly in Indian family-owned businesses. A significant portion of India's top 500 listed entities are family-run, and it's customary for the senior family member to take on the role of Chairperson while grooming a younger family member to become the CEO. Given that these families have most of their wealth intertwined with their businesses, the prospect of bringing in an external CEO or Chairperson becomes unattractive.[40]

Considering the vested interests at play, this intricate situation presented complexities for SEBI's reform agenda, and a more gradual, accommodating approach might have yielded better results. A more lenient stance on the related-party rule could have struck a balance. Nevertheless, it's crucial to acknowledge that the emphasis on separating the CEO and Chairman roles marks a positive step

[39] Jonathan Macey & David F. Larcker, The Chairman-CEO Controversy over Board Leadership Structure, 63 Bus. Law. 697 (2016)

[40] Umakanth Varottil, The Great Divide: Chair and CEO roles B.Q. Prime (2020), https://www.bqprime.com/opinion/sebi-on-separating-chair-and-md-ceo-roles-the-great-divide (last visited September 14, 2023).

forward in enhancing transparency and accountability within corporate governance.

For companies where a single individual holds both the chairperson and CEO positions, a requirement to appoint a lead independent director (LID) should be in place. Even though the Kotak Committee recommended introducing the LID position in India, SEBI has yet to embrace this proposal. In the United States, LIDs emerged as a counterbalance to the combined chairperson-CEO role. They primarily oversee the board's Chairperson, mirroring the Chairperson's oversight of the CEO, and they provide an additional avenue of contact for shareholders. BlackRock's investment stewardship guidelines, practical in 2022, also advocate empowering LIDs to shape board meeting agendas and facilitate separate meetings of independent directors.

VI

Conclusion

In conclusion, while separating the roles of CEO and Chairman has become widely accepted in many Western countries, its implementation in India faces numerous challenges rooted in the country's unique corporate landscape, cultural values, and regulatory framework. Family-centric businesses, concentrated ownership, and the influence of promoters are significant factors that make separation difficult. However, it is essential to recognize that corporate governance is not one-size-fits-all, and what works in one context may not work in another. India's regulatory approach of "comply or explain" acknowledges the need for flexibility while encouraging companies to adopt best practices voluntarily.

Ultimately, the decision to separate the roles of CEO and Chairman should be driven by a company's specific circumstances, its commitment to good governance, and its consideration of the interests of shareholders and other stakeholders. As India's corporate governance landscape evolves, it will be interesting to observe how these roles may adapt and change in response to internal and external pressures.