THE CHAIRMAN’S JOB

A conversation on corporate governance

BY DAVID SNOW

When it comes to corporate governance, what exactly should a chairman do? Where should his or her powers end and those of the CEO begin? What follows is a conversation with Charles (Chad) Holliday, nonexecutive chairman of Bank of America and former chairman and CEO of E.I. du Pont de Nemours & Company, focusing on the responsibilities and best practices of the chairman as distinct from those of the CEO. The conversation was with Robert Hallagan, vice chairman and managing director, board leadership services, Korn/Ferry International. Hallagan is a board member and chairman emeritus of The National Association of Corporate Directors and had conducted research on the topic of corporate governance.

Seated in a Bank of America office in downtown Washington, D.C., Chad Holliday wants to make something perfectly clear: This is not his office. Moreover, he doesn’t have an office.

There is a good reason that the chairman of one of the world’s largest financial institutions is taking pains to clarify this seemingly obscure detail, and it says something profound about an important topic in corporate governance today.

You see, Holliday would like to leave zero room for confusion about his job description, which emphatically is not to run Bank of America. His job is to lead the board of directors of Bank of America. The other job belongs to the bank’s chief executive, who does have an office, as the CEO should.

Holliday’s eagerness to deflect executive aspirations arises from his status as chairman, not CEO, of Bank of America. Before you shrug, remember that at most large United States corporations, those two job titles are joined with an “and.”

Everyone knows what the chairman and CEO is — he, or she, is the person in charge. Far fewer people know what the chairman is when liberated from CEO duties. A silent overseer? A rival? A ceremonial figure? The reason for this lack of clarity is simple — most United States corporations have no history with separated chairman and CEO roles. But history is changing in this regard, and there is a risk that companies are having chairmen thrust upon them before they’ve had a chance to fully learn what a chairman is, what a chairman does, and how to tell if you’ve got a good one or a bad one.

The dichotomy between the two roles is intuitive across Europe and Japan, where separation is nearly universal. To be sure, in the United States, the pressure to split the roles of the chairman and CEO has been growing for years. To the swelling chorus of corporate activists who have demanded the split, opponents have usually argued that the idea is a red herring and won’t in and of itself fix any corporate dysfunction.

Amid the wreckage of the Great Recession, however,
what was previously a gradual trend toward the split model has gained momentum, with Congress, the Securities and Exchange Commission and even the major stock exchanges eying rules that, if enacted, would drastically change the way that most large American companies are led.

Adding to this momentum, Institutional Shareholder Services, the powerful proxy shareholder firm, has proposed adopting a policy for 2011 to almost always vote for a split in the chairman and CEO roles, especially if the company holding such a vote has “problematic performance, governance or management issues,” which describes just about every large American company at some point or another.

Chatting with Chad

It is a certainty that more and more companies will adopt this split model going forward, many for the first time. But too many will do so without an instruction manual for making the model work. To write such a manual, it might be wise to first consult Charles (Chad) Holliday, who knows his way around both roles and is an expert navigator of the space between them.

Holliday. Bank of America’s first nonexecutive chairman, got the job after shareholders voted to strip then-CEO Kenneth Lewis of his chairmanship in April 2009. A year later, Holliday was elected chairman of the financial giant, whose chief executive is now Brian Moynihan. Holliday spent approximately 10 years as chairman and CEO of DuPont, but for stretches he served in each role separately. Today, he also serves as the lead director on the board of Deere & Company, which is led by a combined chairman and CEO, and he sits on the board of Shell, which has separate chairman and CEO roles.

Briefings was a fly on the wall during a recent conversation between Holliday and Robert Hallagan, a Korn/Ferry vice chairman. The talk centered on what Holliday views to be the highest priorities of the nonexecutive chairman, and on how he has structured his relationship with Moynihan in accordance with those priorities. Like Holliday, Hallagan is a serious student of corporate governance, overseeing board leadership services for Korn/Ferry.

Hallagan kicked off the discussion by noting its timeliness, given the many pressures for separation of the roles, and given Bank of America’s high profile as a case study in this regard. “Our interest is in making sure that we’ve really studied the competency model of what makes a good chairman versus a CEO,” Hallagan said. “And we wanted to get your thoughts early on.”

Holliday’s first point put his no-office comment in perspective: Above all else, it is crucial that everyone understand who does what. Referring to his diverse experience at DuPont, Holliday said that “almost anything will work if everybody understands what the roles are. And by everybody, I mean the chair, the CEO, the shareholders, the rest of the board, the employees, the senior management. ... What I find in the European and Japanese system is that everybody understands. Nobody questions the chair’s role.”

With many corporations preparing to enact the same change as Bank of America, Holliday warned that while business success is certainly achievable under the split model, the transition from combined to split models would not necessarily go smoothly for all corporations. Most of the Fortune 500 companies have combined roles, he said, which means that today “people understand what combined means. It’s when you separate it, then you create this lack of understanding and mixed expectations. The CEO [may not] have a role model to look to to just be the CEO; the chair [may not] have a good role model. It leaves the opportunity for confusion.”

Top of the board

Holliday said his messages to the Bank of America community about his role must be consistent and unambiguous. “I am the chairman of the board of directors, not the chairman of B. of A.,” he said. “Brian is the CEO, 100 percent in charge.”

This messaging should be backed up by gestures large and small, like the lack of a permanent office. Holliday also never sends official communications to bank employees. “I think that would be confusing,” he said.

Being the leader of the board means guiding “the effectiveness of the board,” Holliday said. “Which is, do we have the right committees? Are they staffed right? Do they have the processes to get their jobs done as they should? Is the board staffed right? Does it have its processes? Are we getting the information that we need?”

This led to a discussion of specific competencies that nonexecutive chairmen should possess, which may be different from those needed by successful CEOs. “I think the CEO has to have it all,” Holliday said. “I think the chair could maybe be a little bit weak in some pieces. And that sounds negative, but I don’t mean it that way. The CEO has to demand results every day of every week, and there’s a tempo to that. A board just doesn’t operate under that kind of tempo.”

By contrast, a high-functioning chairman should know “how to get groups to work together, how to listen, how to lead an effective meeting, how to keep your mouth shut and
let others talk. It’s leading teams when they don’t really quite have to do what you say.”

While being clear about who runs the actual company, it is, of course, crucial that the chairman communicate effectively with the CEO and that the two are supportive of each other’s goals. This can be murky territory, especially in a company that has just opted for the split model. Several times during the conversation, Holliday and Hallagan acknowledged the fine line between a chairman who vigorously supports the CEO, and a chairman who strays into the CEO’s turf. Holliday keeps a close eye on this line but believes strongly that the relationship he is forging with Moynihan should give the CEO valuable resources to draw on while remaining firmly at the helm of the ship.

Promoted into the CEO job, Moynihan no doubt knew that leadership of Bank of America was going to be highly complicated, but he may also be finding unexpected complexities inherent to the CEO-board dynamic. “What I’ve been trying to do is to help Brian understand some of these things I had to learn,” Holliday said. “It’s hard to tell somebody these things. They almost have to experience it themselves.”

Hallagan added, “The fact that you are the nonexecutive chairman, you don’t want to be too nurturing…”

“I might say it a little differently,” Holliday said. “If it looks to the rest of the board that I’m so much in Brian’s camp that I might not be objective, that might be a problem. So there’s a balance there. If management needs to consider a different approach to something, I’ve got to be able to say that.”

Hallagan pointed out that many boards struggle to give effective performance evaluations to their CEOs, making the informal feedback offered by a nonexecutive chairman all the more valuable. “You need to have a much better way of keeping the CEO attuned to his strengths and weaknesses,” he said.

A chairman has a unique ability to play a mentoring role for the CEO, Holliday said, contrasting this with his experience at Deere & Company. “As lead director, I think I don’t feel quite the latitude to coach the CEO,” Holliday said. “We’re close. I talk to him, but not as frequently as Brian. I will coach him, but I don’t feel quite the freedom.”

As a nonexecutive chairman who was once a CEO, Holliday seeks not only to be a mentor to Moynihan but also to guide him on how to be further mentored. When he was CEO, Holliday himself benefited from the guidance of three undisclosed wise men while at DuPont. “I never told anybody who they were,” he said of his coaches. “They had no relation to the company. They were all highly successful. One of them, I would show him the notes of my senior meeting, and he would say: ‘Well, you didn’t really decide that. Why didn’t you decide that?’ He would sort of push me. I would see them about once every six weeks. I found they were honored to do it. It wasn’t about ego, because nobody knew they were doing it.”

Moyihohan and Holliday speak about once a week, Holliday estimated. The two try to meet in person at least once a month. Facilitating this scheduling exercise is a novel feature of their relationship — the two men share an administrative assistant. “That was Brian’s idea — I wish it were mine,” Holliday said. “She keeps us linked. Brian knows everything I’m doing if he wants to. I can know everything he’s doing if I want to. It’s an openness thing.” If a chairman and a chief executive have separate staffs and separate offices, “it ends up being a wall,” he said. “How much time and effort is spent just to get the two to talk to each other?”

Mixed in to their ongoing agenda items, Holliday tries every week to ask Moynihan at least one question that he isn’t expecting, he said. A recent example: “With which of your senior team do you spend the most time?”

Nurturing, but not too much

Hallagan asked whether Holliday’s lack of experience within the financial industry makes him, in a way, a stronger candidate for nonexecutive chairman — in other words, more likely to focus on board-level improvements and less likely to try to do the CEO’s job. Holliday responded: “It cuts both ways. I’m not going to start second-guessing the business decisions. Yet there is some grounding experience in knowing the industry. At least I have led a large global company,” alluding to DuPont.

He continued: “I can bring to Brian ideas for how to organize and coach him on all the different business organizations. I can bring something to the party, but not financial expertise.”

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A nonexecutive chairman, assigned to run a high-functioning board of directors, can act as a bridge-builder between the senior executive and the board. That becomes all the more crucial when important strategic decisions loom.

To this end, Holliday details a practice he brought to Bank of America from DuPont that he says has been very effective at getting board members up to speed. “When there’s a really critical decision — and there’s really only one or two of these a year — we send a pair of management team members out to meet with a board member in their home or office and cover the issues fully in advance,” he said. “That way, when you get to the actual board meeting, you know what everybody’s issues are, but they’re grounded on the material so you’ve got the time in the boardroom to have a little discussion. It takes a lot of time, but on those critical decisions, I think it’s a fantastic investment. I think it’s a best practice, but I’m biased.”

Asked what he calls this best practice, Holliday responded, to laughter: “At DuPont we called this ‘the pigeons’ because these were like homing pigeons. If one didn’t come back, we’d know it was a bad sign.”

Hallagan clearly liked “the pigeons” technique. “The advantage is when you send them out, the board member knows it is important,” he observed. “It’s showing the right respect for the board member and making sure that they do their homework. It says you want their best thinking.”

Term limits

Part of the argument for separating the roles of the chairman and CEO is that doing so lessens the likelihood that the corporate leader will assume an unchecked and open-ended tenure. In the United States, however, there are no broadly adopted guidelines for the tenure of a nonexecutive chairman. Holliday and Hallagan agreed that these chairman positions should indeed come with term limits. “There needs to be a very easy way to make an exit,” Holliday said. “The expectation ought to be that it’s going away; otherwise it can go to somebody’s head.”

Taking the thought a step further, Hallagan described the ideal chairman as someone who has an incentive to “stay long enough so that you can have an impact, but you know one of your jobs is finding your successor as chair, and making sure the process is in place that you have bench strength on the board. So when you’re recruiting board members, you are thinking long-term, and you start to have board members who have the right competencies to be in that chair role.”

For the record, Holliday estimated that his role as non-executive chairman of Bank of America is a “half-time job,” but a very demanding half-time job. That time commitment should also be taken into consideration when agreeing on compensation, he said.

Indeed, finding a nonexecutive chairman is not a well understood task. The two men noted that many board members are unclear as to what selection criteria to use. Think of how much time and money is spent with CEO compensation consultants, Holliday remarked, and how little is spent designing a superior process for nonexecutive chairman selection. Hallagan added with a rueful chuckle: “Think of the pain that goes into designing the profile for the next CEO, and then think of how little time you spend thinking about separating the role. Everybody just looks around the room. ...”

The conversation ended with another shared observation: describing the ideal nonexecutive chairman is one thing, but designing a formal evaluation for the chairman’s performance is quite another. Hallagan said that most corporations probably do not separately assess chairman and CEO skills where the roles are combined. Therefore, when the roles are separated, these corporations may not have a way to evaluate the chairman in a fashion tailored to the role’s necessary competencies.

Chairmen who are not effectively sized up miss an opportunity to lead by example. “You’re setting the tone that everybody should be held accountable,” Hallagan said. “You say, ‘Here’s the role that we’ve defined for the chairman, so guys, do a 360 around me. Be honest, because I’m getting used to this role.’”

With a smile, Holliday said, “You gave me a good idea.”

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