CHAPTER 2

# Chief Executive Officers

**Abstract** A number of characteristics make the role of a CEO distinctly different from other leadership and management roles. Being a CEO means bearing full responsibility for an organization's success or failure, but being unable to control most of what will determine it; having more authority than anyone else in the organization, but being unable to wield it without unhappy consequences. CEOs' mindsets and strategic beliefs are likely to be instantiated to a significant degree in their firms' current strategies.

**Keywords** Responsibility · Accountability · Charisma · Compensation · Power · Influence

## Introduction

CEO is the only executive at level 1 in the hierarchy of an organization (Carpenter and Wade 2002). All other executives in the organization are at lower levels. At level 2, we find the most senior executives. Level 3 includes the next tier of executives if the organization is of substantial size in terms of the number of employees (Gottschalk 2007). There are various other titles for the top executive in an organization, such as managing director in the UK and administrerende direktør in Norway. However, more and more global companies and other organizations apply the CEO title. This chapter is based on my previous



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book entitled "CIO and Corporate Strategic Management: Changing Role of CIO to CEO" (Gottschalk 2007).

## CEO Power and Influence

CEOs typically enjoy substantial individual freedom in their professions with little or no control. The CEO is the only person at that hierarchical level in the organization. Below the CEO, there are a number of executives at the same hierarchical level. Above the CEO, there are a number of board members at the same hierarchical level. But the CEO is alone at his/her level. The CEO is supposed to be controlled by the board, but the board only meets once in a while to discuss business cases. Executives below the CEO are typically appointed by the CEO and tend to be loyal to the CEO. Therefore, power, influence, and freedom are characteristics of CEOs (Gottschalk 2007).

CEO power and influence can be illustrated by what is labeled CEO fraud in law enforcement. CEO fraud is not fraud by CEOs. Rather, CEO fraud is fraud committed by someone claiming to be the CEO. If someone claims to be the CEO, most people in the organization will do what they are told. As long as they believe that the message stems from the real CEO, they are completely obedient and do as they are told by the fake CEO. The US Federal Bureau of Investigation (FBI) warned in 2016 about a dramatic increase in CEO fraud, e-mail scams in which the attacker spoofs a message from the boss and tricks someone at the organization into wiring funds to the fraudsters. The FBI estimates these scams cost organizations in the USA more than one billion dollars per year. Organizations that are victimized by CEO fraud can be characterized by a combination of CEO power and obedience culture.

Some of the surprises for new CEOs arise from time and knowledge limitations—there is so much to do in complex new areas, with imperfect information and never enough time. Others stem from unexpected and unfamiliar new roles and altered professional relationships. Still others occur because of the frequent paradox that the more power you have, the harder it is to use it. While several of the challenges may appear familiar, Porter et al. (2004) discovered that nothing in a leader's background, even running a large business within his/her company, fully prepare them to be CEO.

CEOs have long been recognized as the principal architects of corporate strategy and major catalysts of organizational change, and the extent to which CEOs can effect change in corporate strategy is thought to be determined largely by the power they possess, and how they decide to apply it (Bigley and Wiersma 2002).

While strategy development as well as organizational change may be at the center of CEO work, many CEOs spend much more time on other—and more minor—matters and issues. Conflicts between individuals in the organization take time to solve, and sudden media attention can steal even more time—and sometimes sleep—from important strategic thinking. Trivial matters tend to occupy much of CEO time.

Many CEOs discover that they are alone, particularly in difficult times. They have nobody at their side on the same organizational level with whom they can openly discuss how to get out of a crisis situation. Rather, others in organization may speculate whether or not the CEO will survive in the position and act accordingly to rescue their own future in the organization. Problem-solving is at the core of CEO work. Mindsets are conceived as distinct cognitive operations that facilitate problem-solving. The concept dates back to the end of the nineteenth century and the experimental psychologist Oswald Külpe, who showed that most of the human thinking happens without images (imageless thoughts), and that most of it also occurs outside of our awareness. The resulting term, "Bewusstseinslage," literally a "state of mind," was later translated into the concept of mindsets, "Einstellung."

Külpe showed that subjects would single out the features related to their tasks, while unimportant or irrelevant features were rejected from their attention. For example, faced with the task of observing the number of letters presented to them, subjects may be totally unable to recall the color and may even deny that color has been experienced at all. This is the original meaning of the term "mindset": The brain is "set" to perceive the world according to predefined criteria. In the course of his research, it was observed that, while given tasks were conscious initially, after a few repetitions the tasks would gradually disappear from consciousness. Upon increased practice, conscious awareness concerning the task waned, although the task could be completed even if there was no awareness of it (Cohen-Kdoshay and Meiran 2007). Subjects had no phenomenological awareness of inner speech at the time of the study, i.e., there was no longer conscious reflection about the tasks. The original purpose is duly forgotten and appearance of the stimulus automatically activated the prescribed conduct.

The word "set" in "mindset" describes how the actor is perceptually prepared or "set" to detect and respond to a given situation (Cohen-Kdoshay and Meiran 2007), a cognitive recognition pattern that is automatically evoked when scanning the environment. The core aspect is that mindsets are (a) caused by repetitive tasks; (b) automatic behaviors set in play with little or no awareness; and (c) replace personality-based dispositions with mindset content. Mindsets can be extremely effective in terms of seizing business opportunities, but are in themselves neither lawful nor unlawful since the ethical implications may not be a part of the mindset. Instead, they may be seen as automated recognition of opportunity with instrumental value as profit maximizing in a competitive setting (Gottschalk 2016).

Bigley and Wiersma (2002) argue that CEOs' cognitive orientation should influence how they wield their power to affect corporate strategy. On the other hand, predictions about a CEO's use of power require an understanding of the CEO's cognitive orientation toward his/her firm's strategy, because power is simply the ability to bring about a preferred or intended effect. Hypothesized association between a CEO's cognitive orientation and corporate strategy presupposes that the CEO has sufficient power to bring about the preferred or intended effects.

At the core of a CEO's mindset, we sometimes find himself/herself. Being alone at the top with rivaling executives as main contacts, the CEO has to enter the role of team player without really believing that it will work. There is no top management team, and the CEO is alone. Over time, a CEO may focus more and more on managing the role rather than managing the company.

Not all CEOs work for change. Some are more committed to status quo—particularly to their organization's current strategy and leadership profile—than others. Hambrick et al. (1993) found that many organizations do not adapt effectively to changes in their environments because of CEO commitment to status quo. Organizational inertia can thus be caused by the CEO, making the organization unable to change at the same rate as its environment. McClelland et al. (2010) found that CEO commitment to status quo is influenced by variables at the individual, firm, and industry levels. Increasing CEO age and tenure is associated with greater status quo commitment. CEOs in firms with financial slack view change more favorably. In contrast, CEOs at firms with liquidity problems may be more committed to the status quo out of necessity.

CEOs' mindsets and strategic beliefs are likely to be instantiated to a significant degree in their firms' current strategies. When a top executive seeking advice confirms and/or restores his/her confidence in the correctness of strategic beliefs, the CEO will be less inclined to alter firm strategy. The mindsets of CEOs are expected to cause them to be the principal architects of corporate strategy and major catalysts of organizational change (Bigley and Wiersma 2002). Belonging to their mindsets is how to use power and secrecy, building alliances with some people and keeping others in the dark about their dispositions, as shown by Bigley and Wiersma (2002). McDonald and Westphal (2003) theorized that relatively poor firm performance can prompt CEOs to seek more advice from executives of other firms who are their friends or similar to them and less advice from acquaintances or dissimilar others and suggests how and why this pattern of advice seeking could reduce firms' propensity to change corporate strategy in response to poor performance.

Similarly, CEOs can have a tendency to listen more to executives in their top management teams who confirm rather than disconfirm their beliefs. Differential association theory postulates that CEO learning occurs in association with those who find their behavior and thinking favorable and in isolation from those who find it unfavorable. Differential association is the process whereby one is exposed to normative definitions favorable or unfavorable to illegal or law-abiding behavior (Sutherland 1949). Whether CEOs engage in white-collar crime is largely based on their socialization within certain peer groups (Holtfreter 2015).

McDonald and Westphal (2003) tested their hypothesis that relatively poor firm performance can prompt CEOs to seek self-confirming advice. The results from a large sample confirm their hypothesis and show that executives' social network ties can influence firms' responses to economic adversity, in particular by inhibiting strategic change in response to relatively poor organizational performance. Additional findings indicate that CEOs' advice seeking in response to low performance may ultimately have negative consequences for subsequent performance, suggesting how CEOs' social network ties could play an indirect role in organizational decline and downward spirals in firm performance.

Johnson (2002) phrased the question: Do CEOs matter? To answer this, he cites two critical dimensions that influence the magnitude of a CEO's impact on an organization. First is resource availability, which is dependent upon an organization's level of debt (higher debt means less cash available to direct toward investments or acquisitions) and level of slack (that is, the number of extra people or amount of assets that the CEO can easily redeploy to take advantage of an opportunity or to avoid a threat). The second dimension is opportunity availability, which is determined by independence, concentration, and growth. CEOs at the helms of organizations with low debt levels and high slack levels—thus high resource availability—will exert more powerful impact on their organizations, and CEO impact increases as opportunities become scarcer.

In the theoretical perspective of principal and agent, the CEO is the agent in a relationship with the board as the principal. Agency theory suggests that agent and principal may be dissimilar in three aspects. First, they may have different preferences and even conflicting values. Next, there is an asymmetry in available knowledge about the organization, where the agent knows much more than the principal. Finally, differences in attitude toward risk may exist, where they have different risk aversion and risk willingness. Because of such differences, the CEO may demonstrate opportunistic behavior by making decisions that benefit himself/herself at the expense of the board as the principal. Agency theory argues that the principal is unable to control the agent because of lack of insight and access to activities performed by the agent in roles such as mayor, chairman, or CEO (Eisenhardt 1985).

Shen (2003) proposed that boards need to focus on CEO leadership development in early CEO tenure and shift toward control of managerial opportunism as CEOs prove their leadership on the job. Shareholders employ some agents in terms of board members. Board members recruit an agent as chief executive officer. The CEO employs a number of top executives. Top executives recruit middle managers. Thus, principals and agents can be found at different levels of corporate hierarchy, and some are both in the role of principal in one relationship and in the role of agent in another relationship.

Most CEO research has tended to take a rather one-sided view of leadership, emphasizing its positive and constructive aspects while avoiding its darker sides. A possible reason for this one-sided attention may be that leadership research has primarily focused on leader effectiveness, strategic thinking, and factors that contribute to optimal performance and results (Glasø et al. 2010). However, there are several dark sides of leadership that merit attention by researchers. One of the darkest sides of leadership is white-collar crime, where the CEO exploits criminal options for corporate and/or personal gain. This constitutes the main topic of our statistical analysis.

However, dark sides of leadership can be found in less severe forms. One example is bullying and harassment, which may or may not be linked to crime. Bullying and harassment by CEOs are reported to happen on a regular basis in many work organizations. Bullying and harassment at work may be defined as repeated behavior, actions, and practices directed at one or more colleagues, which may be conducted either deliberately or unconsciously, but which are unwanted by the targets, causing humiliation, offense, and distress, and which may interfere with job performance and/or cause an unpleasant working environment (Hoel et al. 2010).

CEO power and influence, actions, and decisions are supposed to be monitored by owners, shareholders, or board of directors. Boards of directors are charged with protecting the interests of their companies' shareholders. As such, their primary role is to monitor behaviors and efficacy of company executives on behalf of dispersed owners, alert to the potential honest mistakes and misjudgments, as well as outright misdeeds and white-collar crime. However, Hambrick et al. (2015) found that boards often fail in their monitoring responsibilities. One reason is that many board members are missing some of the following attributes: independence, expertise in the domain, bandwidth, and motivation. To be capable of dispassionate monitoring, a director must be independent and objective about the organization's managers and their policies. Being an effective monitor requires expertise, i.e., in-depth knowledge and understanding of the domain being monitored. Bandwidth means ability to devote requisite time and attention. Directors are selected to the board primarily because of their accomplishments, stature, and connections. Thus, most directors are extremely busy, with significant competing demands on their time and attention.

The fourth and final attribute is motivation, which is defined by Hambrick et al. (2015) as eagerness to exert oneself on behalf of shareholders. Monitoring is hard to accomplish. It requires a director to undertake careful scrutiny and analysis of available information. It also requires a director to ask for additional information, which then requires yet more time and effort and might raise eyebrows. To voice any substantive concerns, an act that fellow directors might see as non-collegial, time-consuming, and even as a provocation, is no easy task at all. The CEO may perceive it as criticism (Tingstad 2016: 28):

> The real challenge lies in each director's courage and willingness to challenge management, ask tough questions and take intractable positions on the board. Such courage could of course mean that you end up in minority position, but also that you are frown upon in the board and among executives, are perceived as problematic, and eventually disappear from the board. Experience, among others from Yara, shows than only a few board members have the courage to move into such a position.

## CEO Responsibility and Accountability

Being a CEO means bearing full responsibility for an organization's success or failure, but being unable to control most of what will determine it; having more authority than anyone else in the organization, but being unable to wield it without unhappy consequences. Porter et al. (2004) make this sound like a very tough job. They argue that this comes as a surprise to CEOs who are new to the position.

It is often argued in business school textbooks that CEO main responsibilities include developing and implementing high-level strategies, making major corporate decisions, and managing overall operations and resources of a company. In terms of time, many CEOs spend most of their time on conflicts that may involve themselves, media, and personal agendas such as headquarter location close to home, company cars, and CEO reputation outside and inside the organization.

An interesting issue is whether or not a CEO is bearing full responsibility for financial crime on behalf of the organization and whether a CEO can be held accountable for corporate crime. Corporate crime, sometimes labeled organizational offending, is resulting from offenses by collectivities or aggregates of discrete individuals (Bradshaw 2015). If a corporate official violates the law in acting for the corporation, it is defined as corporate crime. On the other hand, if he/she gains personal benefit in the commission of a financial crime, it is defined as occupational crime. Occupational crime is for personal benefit, while corporate crime is for organizational benefit.

A corporation cannot be subject to imprisonment, and therefore, the majority of law violations by corporations are legally solved by a fine. For example, Dutch telecommunications company VimpelCom paid $835 million to the US Securities and Exchange Commission and to the public prosecution service of the Netherlands for corruption in Uzbekistan to obtain mobile frequencies in that country. It came as a surprise that Norwegian citizen Jo Lunder, former CEO at VimpelCom, was charged with the company's corruption by the Norwegian national authority for investigation and prosecution of economic crime (Økokrim), although Lunder claimed he had never been involved (Hovland and Gauthier-Villars 2015). Other Norwegian CEOs at that time, such as Walter Qvam, CEO at defense company Kongsberg Group involved in corruption in Rumania, and Gunn Wærsted, CEO at Nordea bank involved in illegal offshore structures for tax evasion and money laundering, were never charged with their organizations' misconduct and crime (Ekeberg 2016).

Accountability refers to liability, answerability, and blameworthiness. Accountability is the acknowledgment and assumption of responsibility for actions and decisions. Accountability refers to situations in which someone is required or expected to justify actions and decisions. Accountability is concerned with holding someone responsible to someone for something (Smith 2009). Accountability implies individual responsibility for misconduct and crime. In accountability processes, sanctions generally function to punish failure, while rewards and awards generally function to commend successful performance.

In rare cases, the CEO is held personally accountable for corporate crime and convicted to prison. Thorleif Enger, former CEO at global fertilizer manufacturer Yara, was sentenced to 3 years in prison in Norway. Enger and three more executives were convicted to prison in 2015. They have appealed their verdicts, and they appeared again in a court of appeals in late 2016 (Barstad 2016). Prosecutors accused the men of knowing about payments of around $8 million in bribes to officials in India and Libya—including to the family of former Libyan leader Muammar Gadhafi's oil minister and the family of a financial adviser in India's Ministry of Chemicals and Fertilizers—for the right to establish joint ventures (Berglund 2015).

After the conviction of the CEO at Yara, Tormod Tingstad, former chief compliance officer at Yara, wrote a note under the heading "A day of happiness?" (Tingstad 2015):

> Should I be happy or sad on a day when four men, current and former Yara executives, are convicted of gross corruption in the Oslo City Court? As it stands today, two to three years imprisonment awaits the four, having been found guilty of corruption in connection with investments in Libya and India.

> I was Chief Compliance Officer of Yara between 2009 and 2013, and lived and worked in the "corruption tsunami" that marred the company in the same period. My job was to protect the integrity of the company, while rendering Norwegian authorities the assistance they required during the investigation. A balancing act, to say the least, I never had an agenda to "get" anyone, but I was the compliance officer for a reason.
>
> On a personal level, today's convictions, sure to be appealed, call for no celebrations. Two of the men, Enger and Wallace, have been my superiors—and friends. I have travelled with Enger and his wife, and stayed in Wallace's house when in Florida. They have both been excellent colleagues, and helped advanced my career. Within Yara, Enger was, and still is, widely considered the "man who created Yara", while what was to follow him never made the same impact. As a former colleague, I wish Enger had a more graceful exit from office.
>
> I also feel sad for Yara today: A company that was the historical, if not always financial, backbone of the proud industry locomotive, Norsk Hydro. Yara was the company that raised from the verge of virtual bankruptcy in the late 90s, to become an industry leader, "The Industry Shaper", just a few years later. Today that success fades somewhat in the shadow of the alleged business methods of its now convicted executive.
>
> I do however feel very encouraged by the determination and ability of the Norwegian authorities, namely ØKOKRIM, as well as the Norwegian courts, to invest substantially in pursuing international corruption well beyond the borders of Norway. We can all have opinions on their approach and ability to strike the right targets, but the contribution to the collective fight against corruption is unquestionable. Hopefully, more countries will follow suit.

Ken Wallace was one of the other convicted executives at Yara. He said in court in September 2016: "I am a good soldier but not the commander." Then the obvious question follows: Who is the commander? The likely answer must be: The CEO.

Thorleif Enger's successor as CEO at Yara, Jørgen Ole Haslestad, remembered very little when he witnessed in a court of appeals against Enger and three other executives. This was on October 26, 2016, where Haslestad was asked a number of questions concerning his knowledge of corruption in Libya and India.

Some CEOs show irresponsible behavior. Rather than exposing socially responsible activities, some CEOs contribute to socially irresponsible activities. Tang et al. (2015) studied corporate social irresponsibility and found that CEO hubris affects negatively corporate social responsibility. They claim that hubris is a prominent character trait of many corporate executives. CEOs suffering from hubris are optimistically overconfident; they overestimate their own capabilities and consider themselves superior to the average person. They have a strong sense of self-sufficiency and expect positive outcomes to emerge even in uncertain environments. Hubris lacks key elements of the narcissistic personality, most notably the continuous need for affirmation and applause. Unlike narcissistic CEOs, hubristic CEOs care less about external recognition gained from being socially responsible.

## CEO Role and Behavior

While research on the effect of CEO behavior on the company's performance remains inconclusive, the investment in top leadership performance and accountability has reached unprecedented heights (Gottschalk 2007). In 2005, the average US CEO's pay for 1 day was almost equivalent to the average worker's pay for 1 year. Citing this figure, researchers call for more studies of the job demands of CEOs. When evaluating the effect of CEOs on company performance in terms of leadership skills, it is argued that a one-dimensional more-or-less perspective is too simple. Just as some CEOs may be related to spectacular growth, as in the case of Steve Jobs, some CEOs may expose the company to spectacular downsides and risks by committing white-collar crime.

Porter et al. (2004) argue that this comes as a surprise to CEOs who are new to the job. Is it possible that CEOs are more likely than other managers and professionals to develop mindsets that are conducive to white-collar crime? Our study below addresses the following research question: What differences might be found between white-collar criminals in the position of chief executive officers versus white-collar criminals in other positions?

Being a CEO involves handling exceptional circumstances and developing a high level of tacit knowledge and expertise. These characteristics and experiences contribute to the accumulation of firm-specific human capital. The time a CEO spends in the position represents a significant investment in firm-specific human capital for both the individual and the firm. The firm invests its resources to compensate the CEO, while the CEO invests his/her productive time. Both parties make these investments with an expectation of future return. Therefore, time is a major factor determining the level of firm-specific human capital investment (Buchholtz et al. 2003).

Being the CEO means being formally accountable and bearing full responsibility for a company's success or failure, but at the same time being unable to control most of that which will determine it. Being the CEO means having more authority than anyone else in the organization, but being unable to wield it without unhappy consequences. Porter et al. (2004) make this sound like a very tough job and argue that the extent of the challenges comes as a surprise to CEOs who are new to the job.

Some of the surprises for new CEOs arise from limitations in time and knowledge: There is so much to do in new and complex areas, with imperfect information and never enough time. Others stem from unexpected and unfamiliar new roles and altered professional relationships. Still others arise according to the paradox that the more power you have, the harder it is to use it. While several of the challenges may appear familiar, Porter et al. (2004) discovered that nothing in a leader's background, even running a large business within his/her company, can fully prepare them to be a CEO.

CEOs have long been assumed to take the positions of architects and catalysts of organizational change. The extent to which CEOs can effect change in corporate strategy is thought to be determined largely by the power they possess and how they decide to wield it (Bigley and Wiersma 2002). Because of the overwhelming workload combined with a need to prioritize own time, convenience is often at the core of CEO thinking.

When assuming the position of a CEO, the new accountabilities arise from several sources, such as time and knowledge limitations, unexpected and unfamiliar new roles, and altered professional relationships. According to the power paradox, the more power one has, the harder it is to use it. And last, but not least, the lack of group identity may make it hard to stay in tune with the values of the larger society. A CEO is normally not an owner and not quite an employee either, but a wielder of powers—necessitating that a certain distance is kept from almost all stakeholders. While several of the challenges may appear familiar, Porter et al. (2004) discovered that nothing in a leader's background, not even running a large business within his/her company, can fully prepare someone to be a CEO. The only certainty is the purpose of the task in hand: to maximize returns on investments and keep the employed capital as lean as possible. However, as Ranft et al. (2007: 677) have observed:

> Holding people accountable for outcomes is quite different from holding them accountable for the behaviors demonstrated to achieve those outcomes.

The focus on accountability is, paradoxically, a means of giving the CEO more discretion to act, since the board entrusts the CEO to find a way. In this setting, declarative knowledge has been shown to be of critical, but limited value. The industry of leadership theories and leadership development gains their legitimization from the need to develop dynamic mindsets, rather than formal, declarative knowledge. A look at the nature of mindsets shows how and why these mindsets may facilitate criminal transgressions in CEOs.

The relationship between the CEO and the board of directors is of central importance in corporate governance. Taking an economic model of man that treats human beings as rational actors seeking to maximize individual utility, agency theory argues that, given the opportunity, CEOs will maximize their own utilities at the expense of shareholders (Shen 2003).

CEO role and behavior is linked to organizational identification at the CEO level. While some degree of organizational identification makes the CEO more successful for the organization (Lange et al. 2015), too much organizational identification can be damaging to the organization (Galvin et al. 2015). There is a growing recognition in the strategy literature of the value in understanding various aspects of CEOs' psychological states given their potential consequences for the firm. Evidence suggests that the chief executive officer's organizational identification, meaning the degree to which the CEO's own identity and his/her perceptions of the organization's identity are tied together or overlap, is a key psychological state of mind to understand, because it may have important performance effects.

Lange et al. (2015) argue that strong CEO organizational identification reduces the agency problem of opportunistic behavior because there is little or no difference between own self-interests and the interests of the organization. Increased organizational identification can be predictive of reduced self-serving outcomes with respect to both compensation and prerequisites. CEOs with higher levels of organizational identification are especially willing to engage in behaviors that help the organization and its members. Organizational leaders with higher levels of organizational identification are apt to be good stewards of their organizations' interests.

Even as CEO organizational identification may have those positive implications for the organization, Lange et al. (2015: 1226) emphasize the possible dark side of the phenomenon:

> Very high levels of CEO organizational identification can have non-beneficial consequences for the firm and its stakeholders when the CEO begins to view certain pro-organizational behaviors as correct and appropriate even if in a broader moral sense they are not.

Similarly, Galvin et al. (2015) emphasize the extreme dark side of organizational identification by discussing narcissistic organizational identification. If a CEO says and believes the statement—"I am the company"—then the organization is up for trouble. Narcissism here means seeing oneself as central to the organization's identity. It is a self-centered form of organizational identification. The CEO may lose his/her independent sense of self and engage in questionable behaviors on behalf of the organization. Narcissistic organizational identification is characterized by the domination of individual identity over organizational identity. CEOs with narcissistic organizational identification feel a strong affinity for their organizations' identities, but as an expression of themselves. They see their own identity as the main reference for understanding what the organization is all about.

## CEO Recruitment and Succession

CEO recruitment and succession is perhaps one of the most crucial events in the management life of any organization because of the substantive and symbolic importance of the CEO position (Gottschalk 2007). CEO replacement has been commonly viewed as an important mechanism for organizational learning and adaptation. A change in CEO can fundamentally alter the knowledge, skills, and interaction processes at the top of a company, and these alterations can in turn significantly influence post-succession firm performance. Zhang and Rajagopalan (2004) studied CEO successions, and the following description of this topic is based on their research.

A distinction can be made between two types of CEO succession—inside and outside. Some have emphasized the role of outside successions in organizational learning and adaptation. However, Zhang and Rajagopalan (2004) argue that research evidence consistently indicates that outside new CEOs rarely succeed in their efforts to improve firm performance. It is plausible that although outside successions bring in new competencies and skills, they are disruptive to firms from a process standpoint, and thus, the enhanced cognitive repertoire may not get translated into improved firm performance. Further, the simple distinction between inside and outside succession does not recognize crucial differences between relay and non-relay inside successions, which may have different implications for organizational learning and adaptation.

In relay succession, a firm identifies an heir apparent to its CEO well in advance of the actual succession event and uses the interval between designation and promotion to groom the heir for the top job. A relay CEO succession has two phases. During the first phase, the organization decides whether or not to designate an heir. During the second phase (the grooming phase), the organization decides whether or not to promote the heir to the CEO position. Both phases offer significant opportunities for organizational learning and adaptation. In the first phase, learning and adaptation occur primarily at the organization level. The firm assesses the availability and desirability of various candidates for the CEO position and evaluates their qualifications in light of key internal and external contingencies in order to decide whether to designate one of them as the heir apparent.

The second phase can be characterized as a two-way learning and adaptation process that occurs both at the individual level of the heir apparent and at the firm level. At the individual level, the heir now has the opportunity to carry out some of the tasks of CEO position and thereby to acquire and enhance position-specific knowledge and develop broader leadership skills consistent with the position. Meanwhile, at the organization level, because one candidate has been designated the heir, the organization can now conduct a more focused assessment of this particular candidate's capabilities (cognitive and interpersonal) and continuously update its evaluation of whether the candidate's capabilities fit the CEO position. It can then use this evaluation to subsequently decide whether or not to promote the heir apparent. In this sense, the grooming phase is also a probation period for an heir apparent.

Contrary to the traditional wisdom that outside CEOs are better equipped to turn around poor performance, research results by Zhang and Rajagopalan (2004) suggest that outside successions do not significantly differ from non-relay inside successions in terms of post-succession firm performance, even under conditions of poor pre-succession performance and/or high post-succession strategic instability. Outside successors are usually prized for their new skills, perspectives, and their willingness to initiate changes. It was been noted in the literature that, relative to inside CEOs, outside CEOs are more likely to initiate strategic changes. Most often, though, previous studies have focused upon the impact of outside CEOs on strategic change rather than on the performance consequences of strategic change. The finding that outside CEOs are more likely to initiate strategic change does not necessarily imply that such change improves post-succession company performance. Because outside successors are more likely to lack firm-specific knowledge, it is harder for them to formulate and implement appropriate strategic change. In addition, outside CEO successions often disrupt organizations, and outside successors find it more challenging to get support from other senior executives within the organization. Therefore, it is not surprising that outside succession may not lead to better post-succession organizational performance.

Certain qualities of narcissism, such as charisma and self-esteem, may help candidates to get promoted to CEO positions. While there is considerable variance in narcissistic tendencies across CEOs, many CEOs have narcissistic personality traits such as self-focus, self-admiration, a sense of entitlement, and a sense of superiority (Zhu and Chen 2015).

In comparing post-succession firm performance following different types of CEO succession, Zhang and Rajagopalan (2004) found the best performance following relay succession. Further, post-succession firm performance did not differ for non-relay inside succession and outside succession. These findings thus highlight the value of a potential new CEO's learning experience (in relay succession) before he/she assumes the CEO position.

Another advantage of relay succession is that temporarily there are two persons—rather than one person—at the top of the organization. In the succession process, there will be four eyes rather than two eyes looking at important matters for the business. In the principal–agent perspectives, the retiring CEO does not have the same freedom for opportunistic behavior when the incoming CEO is preparing himself/herself for the job. Of course, there is the possibility that the incoming CEO shares the same deviant culture with the outgoing CEO. But generally, two persons will have a tendency to control each other rather than to stimulate deviant behavior.

In an earlier study, Zhang and Rajagopalan (2003) classified newly chosen CEOs' origin into three categories—intra-firm, intra-industry, and outside-industry—and examined their firm-level and industry-level antecedents. In their sample of CEO successions, intra-firm succession was positively associated with the presence of an heir apparent and the number of non-heir inside directors. Intra-industry succession was positively associated with strategic homogeneity among industry firms and a focal firm's strategic conformity to industry central tendencies.

Taking a supply-side perspective, prior studies have often used the overall size of a firm as a proxy for the size of the available pool of candidates. It has been argued that large organizations tend to have intra-firm successions because they have larger internal labor markets and thus can find more internal candidates who appear to have the ability to solve critical organizational contingencies. Consistent with this argument, several studies have found that intra-firm succession is positively associated with firm size.

However, Zhang and Rajagopalan (2003) drew upon three theoretical perspectives—the executive human capital, agency theory, and power perspectives—to suggest that the actual pool of qualified candidates for the CEO position within the organization is likely to be much smaller than that suggested by the organization's overall size. First, the executive human capital argument indicates that the requirements of the CEO job are substantially different from those of other organizational positions. This is a position with considerable responsibility for overall firm performance; hence, only a small group of executives with experience at the highest levels of an organization are likely to possess the relevant managerial training to be considered serious candidates for this position. A new CEO is charged with challenging strategic mandates, and the learning process can be both time-consuming and stressful unless the candidate has significant prior senior experience within the organization.

Second, the power perspective suggests that in order to qualify for consideration, an internal candidate needs an established power base, especially in relation to the incumbent CEO and the board of directors. Holding a formal job title like president or chief operating officer as well as board membership often evidences such a power base. Some studies provide empirical evidence that power and politics can limit the potential of even very senior executives from ascending to the CEO position. Finally, from an agency theory perspective, a candidate is more likely to be considered seriously for the CEO position if the board of the organization has relevant information on the candidate's skills, abilities, and knowledge. Interactions with the board help to reduce the adverse selection problem that arises from information asymmetry between a board and a potential successor.

Khurana (2001) discuss why boards often make poor choices when attempting to find the right CEO. He recommends succession decisions that follow six steps:

1. Establish the goals and objectives of the search. Examine the strategic and market challenges facing the company. Identify the leadership skill and attributes necessary to meet these challenges.
2. Carefully select the search committee. Ensure that the search committee has individuals who have a deep knowledge of the organization and its challenges. Ensure that the search committee is diverse in its functional backgrounds and cognizant of its potential biases.
3. Separate the roles and responsibilities of the search firm and the search committee. Enlist the entire board in gathering detailed information about candidates through trusted contacts. Allow the executive search consultant to mediate between the candidate and the company during sensitive compensation negotiations.
4. Define the candidate pool broadly. Encourage less obvious candidates to be considered seriously. Use the succession to break the cycle of selecting conservatively while hoping for change. Choose the candidate who can best meet the long-term objectives of the organization, not the short-term reactions of Wall Street and the business media.
5. Analyze the multiple factors affecting organizational performance. Realize that the CEO is an important element of company performance, but not the only one. Recognize the trade-offs involved in selecting an insider candidate versus an outsider candidate.
6. Choose candidates on the basis of the goals and objectives of the search. Use the requirements of the position in guiding the selection rather than evaluate candidates against one another. Avoid political compromises.

Choosing the right CEO will remain a challenge. Khurana (2001) lists seven pitfalls that are derailing searches for the next CEO: (1) missing the chance for organizational introspection, (2) choosing the wrong search committee, (3) outsourcing critical steps, (4) defining the candidate pool too narrowly, (5) equating candidates with their past organizations, (6) overestimating the value of insider or outsider status, and (7) accepting false assumptions.

## CEO Heir Apparent or None

In sum, these theoretical perspectives can be integrated to define an intra-firm pool of qualified candidates for the position of a firm's CEO, and the heir apparent of the organization is by far the most qualified and powerful contender. An heir apparent is the executive who holds the most senior formal position in a firm's hierarchy (below the CEO) and who has the opportunity to access the task of the CEO. Indeed, there is an implicit contract between an heir apparent and a board. Promoting an heir apparent to CEO represents a rule-bound behavior, and breaking this contract can signal instability and uncertainty in a succession process. Given the seriousness of this contract, a firm's board is likely to have obtained and evaluated information about the competencies of a candidate (the organization's heir apparent) prior to approving the appointment. This, in turn, means a significant reduction in the information asymmetry between the board and the heir apparent. Although these factors increase the likelihood of an heir apparent being promoted, Zhang and Rajagopalan (2003) refer to a study where nearly one-third of the heirs apparent in the sample were not promoted. Power struggles and politics often determine an heir apparent tenure outcome; hence, being an heir apparent does not guarantee promotion. These arguments lead to the hypothesis formulated by Zhang and Rajagopalan (2003) that the presence of an heir apparent will be positively related to the likelihood of intra-firm succession.

In addition to the pool of candidates in the intra-firm market, there is a pool of candidates in the intra-industry market. Potentially, a pool of industry candidates for succession to a particular CEO position is quite large, depending on the number of firms within the focal firm's industry and the number of senior executives within these firms. Zhang and Rajagopalan (2003) drew upon institutional theory and executive human capital to argue that the actual pool of qualified candidates within an industry is likely to be restricted to senior executives from similarly sized or larger organizations and from strategically homogeneous organizations.

Institutional theory assumes that there is a willingness of individuals and groups to follow predetermined and acceptable patterns of behavior that are supported by the environment. Organizations seek to enhance and protect their legitimacy by adopting industry practices and norms. Recruiting a new CEO is a particularly visible event; hence, it provides a significant opportunity to communicate an enterprise's intention to conform to or deviate from industry practices. Studies grounded in institutional theory indicate that firms are more likely to imitate other industry firms that are similar in size to them, or larger. In addition to conferring increased legitimacy from an institutional perspective, the hiring of a senior executive from a similarly sized or larger firm is also appropriate for other reasons. First, organizations of similar size are often similar in terms of structural complexity, often rely on similar environmental resources, and often face similar structural constraints. Second, senior executives in relatively large firms also have higher visibility than those in smaller firms, so they are more likely to attract the attention of firms seeking CEO successors and executive search firms. Finally, in addition to enhancing legitimacy from a symbolic standpoint, successors' ties to similarly sized and larger organizations in a business area or government sector also have strategic value for focal organizations because such ties expand the latter's inter-organizational knowledge networks. Thus, the potential pool of organizations with its sector firm which a focal organization is likely to hire its CEO is most likely restricted to those that are of a similar or larger size. Accordingly, the fourth hypothesis suggested by Zhang and Rajagopalan (2003) says that the number of similarly sized and larger firms in an industry will be positively related to the likelihood of intra-industry succession.

The pool of qualified intra-industry candidates can be further narrowed to senior executives in strategically homogeneous organizations by drawing upon arguments from an executive human capital perspective. The extent to which an intra-industry candidate can transfer his/her skills to another organization is likely to depend on the extent of industry homogeneity. This is because executives in homogeneous industries better understand technologies and procedures employed within their sectors as well as the business areas within which the focal organization is active. Hence, although outsiders generally possess less organization-specific human capital than insiders, the magnitude of this difference—and therefore the relative costs of inside and outside succession—is likely to be lower in sectors comprised of homogeneous organizations than in more heterogeneous sectors.

In line with this argument, Zhang and Rajagopalan (2003) formulated a fifth hypothesis that strategic homogeneity among similarly sized and larger firms in an industry will be positively related to the likelihood of intra-sector succession.

Turning to the demand side, it would be expected that a successor CEO's industry origin could be influenced by the extent to which the hiring firm values industry-specific skills and experience. Zhang and Rajagopalan (2003) draw upon strategic contingency theory to argue that one key demand antecedent that makes intra-industry hiring desirable is firm strategic conformity, or the extent to which a firm's strategy adheres to the central tendencies of its industry. Firms that adhere to industry central tendencies are more likely to value industry-specific skills than firms that deviate from industry practices. In firms whose strategies conform to their industries' central tendencies, the critical skills for successors are familiarity with those industries' strategies and practices. In contrast, firms with novel and unique strategies that deviate from industry tendencies are more likely to desire successors who have the ability to explore and evaluate a range of competitive behaviors beyond those that most firms in their industries have already adopted. These arguments lead Zhang and Rajagopalan (2003) to their sixth and final hypothesis that firm strategic conformity to an industry's central tendencies will be positively related to the likelihood of intra-industry succession.

In their empirical study to test these hypotheses, Zhang and Rajagopalan (2003) classified the origin of a new CEO into three categories: intra-firm, intra-industry, and outside-industry. Intra-firm succession was defined as one in which an executive with firm tenure of at least 2 years had been promoted to the CEO position. Similarly, intra-industry succession was defined as one in which the successor CEO had firm tenure of less than 2 years but had industry tenure of at least 2 years in the same industry that the hiring firm was in. Outside-industry succession referred to a succession in which the successor CEO had industry tenure of less than 2 years in the same industry. Among the 220 succession, there were 132 intra-firm successions, 43 intra-industry successions, and 54 outside-industry successions.

Hypotheses 1, 2, 5, and 6 were supported in their study:

**Hypothesis 1** The presence of an heir apparent will be positively related to the likelihood of intra-firm succession.

**Hypothesis 2** The number of non-heir inside directors will be positively related to the likelihood of intra-firm succession.

**Hypothesis 5** Strategic homogeneity among similarly sized and larger firms in an industry will be positively related to the likelihood of intra-industry succession.

**Hypothesis 6** Firm strategic conformity to an industry's central tendencies will be positively related to the likelihood of intra-industry succession.

Hypotheses 3 and 4 were not supported:

**Hypothesis 3** Prior strategic persistence by a firm will be positively related to the likelihood of intra-firm succession.

**Hypothesis 4** The number of similarly sized and larger firms in an industry will be positively related to the likelihood of intra-industry succession.

Zhang and Rajagopalan (2010) published a new study of CEO origin, strategic change, and firm performance. Based on longitudinal data on the tenure histories of 193 CEOs, they found that the level of strategic change has an inverted U-shaped relationship with firm performance. Further, they found that the inverted U-shaped relationship differs between firms led by outside CEOs and those led by inside CEOs. That is, both the positive effect of strategic change on firm performance when the level of change is relatively low and the negative effect of strategic change on firm performance when the level of change is relatively high are more pronounced for outside CEOs than for inside CEOs.

In another study, Zhang (2005) examined how the presence of non-CEO executives, such as a COO and president, who are separate from the CEO, affected strategic change and CEO dismissal. With longitudinal data on the tenures of 207 CEOs, results suggest that the presence of a separate COO or president increases the magnitude of strategic change under conditions of low organizational performance, but it decreases the magnitude of strategic change under conditions of high organizational performance. In addition, the presence of a separate CEO or president increases the likelihood of CEO dismissal under conditions of low organizational performance, and this effect is stronger when the magnitude of strategic change is high; but it has no impact on the likelihood of CEO dismissal under conditions of high organizational performance. These results suggest that the impact of the presence of a separate COO/president on strategic change and CEO dismissal varies across different organizational contexts.

There can be two separate roles of a CEO/president: one representing an heir apparent in training for the CEO position and the other representing a co-leader delegated with internal operating authority (Gottschalk 2007). From a co-leader perspective, it is argued that the decision to have a COO represents a major structural choice: It explicitly divides between two people a set of top-level roles that are typically fulfilled by one person; it draws a structural distinction between strategy formulation and implementation; it adds an organizational layer; and it adds a highly paid executive position to the organization's costs. From a succession (heir apparent) perspective, it is argued that many organizations identified an heir apparent in the COO and/or president position in advance of the actual succession event and used this position to groom the next CEO. Findings of Zhang and Rajagopalan (2003) suggest that the presence of a separate COO/president increases the likelihood that a new CEO will be selected from within the organization. Their study suggests that a CEO and a COO/president in general are partners, considering that as co-leaders, they work closely in their positions and from a succession perspective, it is likely that the CEO will pass the leadership baton to the COO/president when succession occurs.

On the other hand, however, the relationship between a CEO and a COO/president (as a co-leader or heir apparent) can involve rivalry. From the perspective of power circulation and distribution, the number of inside directors on the board might increase the likelihood of CEO turnover under conditions of poor organizational performance. From the perspective of power contestation and rivalry, the proportions of non-CEO inside directors and non-CEO executives might have significant influence on the likelihood of CEO dismissal—often followed by inside succession. Therefore, other senior executives can be power contenders to the CEO. Thus, a COO/president, as a co-leader who is only one step from the top post, can be a power contender to the CEO as well as a controller against CEO misconduct and crime.

Studies from a succession perspective have similar suggestions (Zhang 2005). For example, a CEO may have complex feelings toward a COO/president. While selecting a COO/president as an heir apparent gives the CEO opportunities to continue his/her influence over the strategic direction of the organization, naming an heir apparent also reminds the CEO of his/her own mortality. Especially when the heir apparent is appointed by the board of directors without substantial input from the current CEO, he/she may feel reluctant to cooperate with the heir apparent. In addition, from the point of view of the COO/president as an heir apparent, he/she may become impatient under the shadow of the CEO and wants to be independent with power and influence. The relationship between a CEO and a COO/president might have built-in, and therefore endemic, hazards that are exacerbated rivalry and corresponding defensiveness.

The results of Zhang's (2005) study contribute to building a contingency view on the CEO-COO/president relationship. The findings suggest that the role of a COO/president with regard to a CEO is context-specific. While a COO/president in general is partner to a CEO, the COO/president may become a contender to the CEO under conditions of low organizational performance. Thus, examining the role of a COO/president with regard to a CEO without taking into account the organizational contexts may underestimate the complexity of their relationship. These arguments and empirical evidence also contribute to the understanding of the power circulation and power contestation within political coalitions. By focusing on the two top posts (a CEO and a COO/president), the study suggests that the relationships between the key members of dominant political coalitions vary across different organizational conditions of high firm performance, and organizational adaptation is achieved by their rivalry under conditions of low organizational performance.

A description of rivalry can be found in the book by Erin Callan Montella who was the chief financial officer (CFO) at Lehman Brothers. The bank collapsed shortly after the following episode occurred (Montella 2016: 175):

> In any event, I don't remember doing anything when I came into my office other than sitting at my desk, sipping some coffee, and waiting for the meeting. As it got closer to 7:30 a.m. my fellow executive committee members began to file past my office toward the conference room. It was next to my office so they could not avoid me. But, trust me, no one looked at me. They couldn't make eye contact. You'd think I'd be the one who couldn't look up from my desk, but it was the other way around. I was "dead man walking". No one wanted to go near me. I didn't want to go in there, though, until I thought everyone was seated. There was

> absolutely no way I was going to sit in there and make small talk until Dick showed up. When it seemed everyone was likely there, I walked in and took my regular seat by the window in the middle of the table. In the middle of the action, as I always thought. The perfect spot to be engaged and relevant, or that was the idea.
>
> Dick came in and sat down next to me. He started talking right away, announcing that Joe Gregory and I were resigning from our respective roles. And the scene blurs, like the fade-out in a movie. I know I started to cry. I wasn't outright bawling, just quiet tears down my face. I really did not want to cry. So stereotypical. I never cried about anything. But that was when it hit me. I was no longer the chief financial officer at Lehman Brothers.

Richard "Dick" Severin Fuld was CEO at Lehman Brothers. The bank filed for bankruptcy in 2008. Two years later, an internal investigation into misconduct and crime at Lehman Brothers was carried out by Valukas (2010).

The findings of Zhang's (2005) study also contribute to a better understanding of the inner workings of corporate elites in general. Many studies using an upper echelon perspective have treated corporate elites as a team. A team implies that they cooperate, and all work in the same direction to the benefit of the organization. As a team, the top management group is open to each other and share their thoughts and ideas. As a team, they help each other out. As a team, they have shared understanding of goals and strategies. As a team, they agree on priorities and resource allocations.

However, there are studies emphasizing conflict and competition within corporate elites. While these studies have extended our knowledge of collaboration versus competition within corporate elites, Zhang (2005) argues that we so far know little about the conditions under which top management groups are more likely to be collaborative as a team and the condition under which they are more likely to be competitive. We know that all levels of managers are trying to balance their loyalties to subordinates versus superiors. In top management groups, many executives will perceive themselves mainly as representatives of their respective divisions and departments rather than as participants in the overall management of the organization.

The results of Zhang's (2005) study suggest that corporate elites are more likely to be collaborative as a team under conditions of high organizational performance because they can benefit from the high performance, and they have developed equilibrium in their interests and power. In contrast, under conditions of low organizational performance, change is expected and the prior equilibrium is disappearing, so competition within corporate elites will rise until a new equilibrium is formed.

Further, the findings of Zhang's (2005) study contribute to our understanding of the monitoring within corporate elites. While most studies in the literature have focused on monitoring from higher to lower levels of management, this study is one that has examined monitoring in the other direction—from lower to higher levels of management. The study found that the presence of a separate COO/president increases the magnitude of strategic change and the likelihood of CEO dismissal under conditions of low organizational performance. Thus, the presence of a separate COO/president represents a healthy antidote to the trend toward celebrity CEOs. However, it should be noted that the monitoring from lower to higher levels of management occurs only under conditions of low organizational performance. Such context specificity is not surprising given that higher levels of management (e.g., a CEO) are more powerful than lower levels of management (e.g., a COO/president) in most circumstances.

Carpenter and Wade (2002) developed a theory wherein the pay of non-CEO executives can be explained by micro-level opportunity structures—the intersection of functional position, CEO background, human capital, and firm strategic resource allocation decisions. The theory suggests a positive association between pay and a position made visible by resource allocation decisions, a functional background similar to that of the CEO, and a position that helps the firm manage strategic resource allocations.

In their empirical study, Carpenter and Wade (2002) found that executives received greater cash compensation when they occupied positions in which they were likely to be associated with strategic resource allocation choices made by their firm and when they had functional responsibility similar to the background of the CEO. It is often assumed that executives, primarily CEOs, are compensated for the criticality of the tasks that they must manage. An alternative explanation is the labor market for CEOs. Successful young men—and some women—climb the corporate latter in their 30s and enter into top positions in their 40s. Headhunting firms and other recruiting agencies are aware of new talents and candidates. Headhunters tell candidates what they can and should expect in top positions. When they become CEOs and read in the media about other CEOs who are better paid, they ask for even more money or threaten to leave. While media coverage of very high CEO salaries seems intended to create some moderation, it often has the opposite effect: Those who are below average ask for better pay.

It is reasonable to expect that compensation criteria for CEOs extend to some extent to the pay of other executives throughout an organization. However, although that perspective has typically emphasized external and macro-level determinants of pay (that is, environment, firm size, and corporate strategy), Carpenter and Wade's (2002) study show how the many faces of firm strategy (actions and resource allocation choices) may result in different internal resource dependencies, and thus have different pay implications for particular executives. Furthermore, the study show that executives themselves vary in the position and human capital requisite to managing the contingencies arising from differences in leadership (like CEO background) and strategic resource allocations. Consequently, functional position, along with education and work experience, create certain micro-level opportunity structures that executives convert into higher pay.

Carpenter and Wade (2002) characterize strategy as the pattern resulting from a stream of resource allocation decisions. Such a pattern is comprised, for instance, of an organization's resource allocation choices in research and development, marketing, diversification, capital investments, and international markets. This view follows the strategic choice perspective wherein organizations are under considerable constraints imposed by their environments, but also having some latitude in their actions. Those actions, in turn, may generate fundamentally different ways of allocating resources, as revealed by differences in patterns across organizations. In the context of their study, Carpenter and Wade (2002) argue that such fundamental differences between organizations are likely to create compensation differences among executives within organizations.

## CEO Charisma and Celebrity

There is some degree of controversy concerning whether it is possible for top-level leaders to have a substantial effect on the overall performance of the organizations they lead (Gottschalk 2007). On the one hand, some have heralded leadership on the part of CEOs as an important ingredient for the revitalization of organizations, and as critically important to the top management of large organizations and, in the political area, of nations. On the other hand, proponents of external control assert that CEO leadership is inconsequential to organizational performance. Much of their reasoning is based on the notion that leadership is a perceptual phenomenon that allows observers to develop simple causal explanations for complex organizational events and performance (Waldman and Yammarino 1999).

CEO charisma represents a potentially key component of strategic leadership. Charisma is defined as a certain quality of an individual by which he/she is considered extraordinary and treated as endowed with superhuman or exceptional powers or qualities. Charismatic authority arises from the charisma or gift of grace of the leader. It is up to the followers to recognize this characteristic in leaders and to act accordingly (Aguilera and Vadera 2008).

Charisma is based on behavioral tendencies and personal characteristics of the CEO, including the articulation of a clear vision derived from firmly held values or moral justifications, role modeling of those values, communication for high-performance expectations, and confidence in followers' abilities to meet those expectations, references to the greater collective and its identity, symbolic behaviors, and the assumption of personal risks and sacrifices. CEO charisma involves a relationship between a CEO and one or more followers in close organizational proximity, combined with favorable attributions, primarily from followers at distant organizational echelons, which often results in internalized commitment to the vision of the leader, exceptionally strong admiration and respect for the leader, and identification of followers with the leader, the vision, and the collective forged by the leader (Waldman and Yammarino 1999).

Glasø and Einarsen (2008) studied emotion regulation in leader–follower relationships. They found that negative emotions such as disappointment, uncertainty, and annoyance are typically suppressed while positive emotions such as enthusiasm, interest, and calmness are typically expressed or faked. When leaders and followers referred to experienced or expressed emotions, the most highly scored emotions were "glad," "enthusiastic," "well," and "interested." The reported level of emotion regulation was higher for leaders than for followers.

Leaders tend to be more domineering and assertive, and less social avoidant, distrustful, and exploitable than followers. Glasø et al.'s (2010) study shows that 30% of the leaders exhibit elevated profiles of personality characteristics regarding interpersonal problems, on a level comparable to that of a sample with psychiatric patients, thus, indicating that severe problems may arise in social interactions between leaders and followers.

According to Padilla et al. (2007), there are two types of destructive followers: conformers and colluders. Conformers go along with destructive leaders out of fear, whereas colluders enthusiastically engage in destructive behaviors. Although both groups are motivated by self-interest, their concerns differ (Higgins 1997). Conformers try to minimize any consequences of not behaving as expected, while colluders seek personal gratification via their relationship with a destructive leader. Conformers are motivated by basic needs that are unmet, negative self-evaluation, and psychological immaturity. Colluders, on the other hand, are ambitious, selfish, and share the values of the destructive leader.

Many CEOs attempt to be or are in fact charismatic. Charisma is an ideal-typical form of authority, resting on the devotion to a fascinating character of an individual person. Charismatic leaders have effects on followers through the social influence process of identification. Charismatic leaders typically express symbolic and emotionally appealing behaviors (Fanelli and Misangyi 2006).

Waldman and Yammarino (1999) present a model of CEO charismatic leadership in organizations and show how such leadership can, through levels of management and analysis, impact organizational performance. They suggest that charismatic leadership will result in heightened work efforts by organizational members, which in turn will improve organizational performance.

CEO celebrity arises when journalists broadcast the attribution that a firm's positive performance has been caused by its CEO's actions. In this definition, celebrity has three core components. First, journalists broadcast such attributions through the print and electronic mass media. Second, the attribution involves the causes of a firm's actions that lead to its positive performance. Third, firm actions (and, by implication, performance) are attributed to the CEO's volition. That is, celebrity does not involve attributions to other factors such as luck, environmental conditions, or the actions of other individuals and teams in the organization. Thus, celebrity does not necessarily arise if performance is attributed to a CEO's actions that are portrayed as lucky or dictated by the CEO's environment.

There is a tendency of journalists to attribute an organization's actions and outcomes only to the CEO. Journalists tend to celebrate a CEO whose organization takes strategic actions that are distinctive and consistent by attributing such actions and performance to the organization's CEO rather than to broader situational factors.

A CEO who internalizes such celebrity also will tend to believe this overattribution and become overconfident about the efficacy of his/her past actions and future abilities. Hubris—a personality quality of extreme or foolish pride or dangerous overconfidence—arises when CEO overconfidence results in problematic firm decisions, including undue persistence with actions that produce celebrity. The more those others provide an individual with attributional accounts, the more likely it is that the individual will adopt the view expressed by others. The more a CEO interacts with others who also accept his/her celebrity, the more likely he/she will accept the celebrity attribution as true (Hayward et al. 2004).

Chief executives as heroic figures have been central to leadership theory for a long time, stimulating modern-day neo-charismatic theories such as transformational theory (Arnulf and Gottschalk 2013). A growing concern about dangerous and derailed leadership led to sharp criticism of this heroic picture of leaders. Omnipotent, self-centered CEOs are prone to destructive leadership behaviors and bad decision-making, targeted by criticism from a host of prominent leadership researchers, who equivocally warn that depicting leaders as heroic and treating them as celebrities, is stimulating a dangerous illusion.

Heroic CEOs with charisma and celebrity status are hard to challenge, even when they show misconduct on a slippery slope. People are loyal and look another way. They find explanations why it is acceptable for the CEO to do what he/she does. They ignore negative information and absorb positive information about the CEO that confirms their view of a heroic CEO.

## CEO Content and Context

Organizational research has a long history of examining the association of executive characteristics with organizational decisions and attributes. In the following, some of the commonly examined attributes of CEOs are presented based on research by Barker and Mueller (2002).

First, there is CEO tenure. Researchers examining CEO tenure find that CEOs make fewer changes in strategy as their tenure increases. This lack of change might occur because with each increasing year of tenure CEOs become more strongly committed to implementing their own paradigm for how the organization should be run. Longer-tenured CEOs may lose interest in implementing organizational changes as their outside interests increase and the novelty of the CEO's job decreases. Longer-tenured CEOs may lose touch with their organizations' environments and therefore may not make the changes and investment decisions to keep the organization evolving over time. Longer-tenured CEOs may choose deviant behaviors in business crises to rescue themselves and the organization, since they are not up to date on strategic changes that could solve the problems.

Next, there is CEO age. One of the most enduring findings about executive age is that older executives tend to be more conservative. Empirical studies have found that older top managers (as opposed to younger managers) follow lower-growth strategies. Several psychological reasons are commonly offered for this pattern of findings. Older executives may have less of the physical and mental stamina needed to implement organizational changes. Based on learning theory, older executives may have greater difficulty grasping new ideas and learning new behaviors. Executives in their 40s tend to be the most ambitious where they typically still are promoted to higher positions. They have ambitions on behalf of the organization, behalf of their positions, and behalf of themselves personally. They work hard and sometimes deviant to reach goals for the organization, for the position, and for themselves.

Third, there is CEO education. The education levels of tip managers have been studied. It was found that more educated executives have greater cognitive complexity. It is generally assumed that such cognitive complexity provides greater ability to absorb new ideas and therefore increases the tendency toward accepting innovations. More innovative organizations tend to be led by CEOs who have higher levels of education. In addition to educational level, there seem to be differences between educational fields of study. Focusing on business education and the MBA degree in particular, theorists and critics have argued that MBA programs attract conservative, risk-averse students and teach analytic skills geared toward avoiding big mistakes or losses. Given this description, MBA programs are perceived as doing little toward developing innovative or risk-taking skills in students. On the other hand, avoiding mistakes may also include avoiding misconduct and crime.

Barker and Mueller (2002) applied these three CEO characteristics to explain variation in firm R&D spending. For example, they suggest that CEOs with business or legal academic training may be less inclined to pursue innovation through R&D spending.

The failure and subsequent departure of a CEO is a costly misadventure for any organization. According to Conger and Nadler (2004), the most immediate and devastating impact is often on the company's market capitalization. In a matter of weeks, a floundering CEO can destroy a market valuation that has taken a decade to build. In addition, ousted CEOs rarely leave with empty pockets (Gottschalk 2007).

Conger and Nadler (2004) think of CEOs as broadly oriented in favor of content or context. The distinction might reveal a common pattern in cases of early-tenure CEO failure. Content-oriented CEOs focus on the substance of the company's business. Their interests and capabilities relate to corporate strategy, the core technology of the business, financial structure and performance, and business portfolio changes. In contrast, context-oriented CEOs focus more intensely on the environment in which content decisions are made. They are concerned with values, purpose, the interactions of the executive team, the engagement of leadership across the enterprise, the culture of the organization, and the processes that influence and shape these factors.

Conger and Nader (2004: 54) argue that this CEO characteristic—either content-oriented or context-oriented—might strongly influence the success or failure of a CEO succession:

> Now consider what happened in several instances in which an outstanding context leader was replaced by a content leader. Henry Schacht at Lucent, Paul Allair at Xerox, and John Pepper at Procter & Gamble were particularly good at creating collegiality at the top, building an executive team, engaging the organization, emphasizing values, and forming connections with many people in their companies. They also chose as their heirs apparent individuals with strong content orientations, people with the intellect, strategic insight, and analytic capabilities to complement their own strengths very effectively.
>
> Once the incumbents departed, however, and the new CEOs suddenly had to create a new context on their own, trouble started. Their lack of interest in context or inability to create the right one was problematic. They were unable to build and manage the necessary network of relationships inside and outside the organization. As a consequence, they were unable to engage the top team, build the collective intuition of the leadership group, create an environment in which others felt free to express dissenting views, and so on.

> Faced with performance shortfalls and disappointments, these content-oriented CEOs typically engaged in a cycle of failure. They became more entrenched in their search for the right answer and their belief in the power of that answer. They tended to pay even less attention to context and grew more detached from the reality of the team and organization they were leading.

Conger and Nadler (2004) argue that just as outgoing chief executives, their boards, and incoming leaders bear part of the responsibility for the early-tenure flameouts of new CEOs, so too can they all be part of the solution. They argue that outgoing CEOs can start by bearing in mind that a truly successful legacy is one in which their successors flourish.

## CEO Conflict and Competition

Following a power perspective, Shen and Cannella (2002a, b) studied antecedents of CEO dismissal followed by inside succession. Their theory highlights interest conflicts and competition within top management. They propose that CEO origin, CEO tenure, non-CEO inside directors, and senior executive ownership are important antecedents of CEO dismissal followed by inside succession. Evidence from a sample of 387 large US corporations suggests that non-CEO senior executives frequently play an important role in CEO dismissal.

CEO origin refers to whether an incumbent CEO was an employee of the organization he/she leads at the time of appointment as CEO. Origin has important implications for power dynamics within top management groups. Building strong social networks and coalitions within an organization is an essential task for those who aspire to be the CEO. When they are promoted to a CEO position, inside successors not only have the approval of outside directors, but also have support within the top management group—though perhaps not complete support, owing to internal competition. In contrast, when outside CEOs take office, they lack the internal social network and coalition of inside CEOs.

Accentuating this problem is the fact that senior executives from an organization's prior regime often have a hostile attitude toward outside CEOs because of the changes these outsiders may initiate. While the senior managers tend to express enthusiasm toward incoming CEOs from the outside, saying that they really appreciate new ideas and new approaches, they reluctantly applaud actual changes that outsiders initiate. The symbolic enthusiasm—based partly on a survival instinct—is soon overshadowed by resistance to change. This kind of miscommunication makes it even harder for an outsider to become a successful new CEO.

In addition, because outside successors are often appointed in periods of poor performance and are expected to turn their organizations around, they are under pressure to take quick action in restructuring top management groups. This intensifies interest conflicts between outside CEOs and senior executives who will attempt to distance themselves from responsibility for past poor performance. Remaining senior executives will again talk enthusiastically about new blood and new ideas, while at the same time try to stay passive in a survival mode during initial periods of change. They may think it is smarter to do nothing than to make possible mistakes. For the new CEO, the result may be that he/she get little done because of the passivity in the inherited top management team.

Thus, compared to inside succession, outside succession increases tension within a top management group and places the outside CEO at a higher risk of power contests with senior executives. The high expectations the board and other stakeholders have toward outside CEOs make them more vulnerable when challenges from senior executives emerge (Shen and Cannella 2002b).

If the outside CEO chooses to fire senior executives, the result is quite uncertain. Some senior executives may have ties to board members that the outside CEO did not know. Some senior executives may enter into conspiracies to get the outside CEO removed. Some senior executives may involve the media in spreading rumors and misconduct accusations about the new CEO. If the board lets the outside CEO fire all senior executives, previous informal information flows disappear, and the agency problem for the board becomes more serious. The new CEO established a one-person power base that opens up for opportunistic behavior, misconduct, and potential white-collar crime with a board having no way of noticing.

New CEOs confront significant challenges upon taking office. Promotion to the CEO position typically leads to significant changes in both executive responsibility and task environment. New CEOs must adjust to their new roles and quickly develop good working relationships with the other members of their top management groups, boards of directors, and powerful outside stakeholder. The learning process is stressful and time-consuming. At the same time, new CEOs are charged with specific mandates, a charge that further increases the difficulty of their tasks. Finally, and perhaps most crucial for new CEOs, is their need to establish their authority in a top position.

Every new CEO—whether from inside or from outside—knows that it is a risky position to be in, and that falling from the top is a long way down. Many relationships—which may seem to be friendships—are based on the position and not the person. Loss of the CEO position means loss of membership in the elite and loss of symbolic friends. To keep the position can become a desperate fight against the clock for a new CEO. Misconduct and crime becomes sometimes the only option to secure continued support from the board of directors.

Authority is legitimate power and is of two types—authorized power and endorsed power. Authorized power is granted by those superior to the power holder, and endorsed power is granted by those subordinate to the power holder. To establish their authority, new CEOs must be accepted by both their boards of directors and subordinate executives. Outside board members have other external obligations and would like new CEOs to establish their authority without much involvement from the board. Outside board members would like to spend less time on each board position and prefer CEOs to handle their situations on their own. They dislike learning of internal conflicts or other matters where CEOs need support from their boards.

Although the official appointments represent authorization by boards of directors, it does not necessarily confer endorsement from subordinates. Subordinates may have negative opinions about board members and distrust their choice of new CEOs. Furthermore, the authorization of a board is likely to be somewhat tentative and can be revoked quickly if directors develop significant concerns about a new CEO's leadership capacity. Indeed, because there is little proof of accountability in office, the leadership capacity of new CEOs is under close scrutiny by outside directors. Thus, Shen and Cannella (2002b) argue that until they can prove their competence and meet the expectations of both their boards and subordinate executives, the authority of new CEOs will be much weaker than that of established CEOs.

Inside directors—a practice found in the USA and some other countries—are directors who are also executives of the firm on whose board they serve. Although the effectiveness of inside directors in governance has been widely questioned, since they are supposed to control themselves, theories emphasizing managerial interest conflicts and competition suggest that the presence of non-CEO inside directors has important implications for the power dynamics within top management. First, inside directors are the most likely and viable challengers of a CEO. A seat on the board gives an executive exposure to outside directors and enables them to build social networks and coalitions on the board. This development narrows the power gap between them and the CEO and lends them more confidence with which to challenge the CEO. In cases of CEO misconduct and crime, non-CEO inside directors can more easily bring their suspicions to the board's attention.

Second, for senior executives successfully to challenge a CEO and to advance their careers, they must be able to voice their concerns about the CEO to the organization's board. This may relate to poor decision-making, human resource mismanagement, or other matters.

Finally, the presence of non-CEO inside directors limits a CEO's influence over a board and increases the chance for senior executives successfully to challenge the CEO. Inside directors have valuable firm-specific information about an organization's activities and market position (Shen and Cannella 2002a, b).

Haveman et al. (2001) studied how regulatory punctuations impact CEO succession. Regulatory punctuation is a type of environmental discontinuity that is sudden and represents extensive shifts in constraints on business operations. Regulatory punctuations alter both technical and institutional features of organizational environments. They can alter technical environments by raising or lowering barriers to entry. They can also set prices or eliminate price controls. Regulatory punctuations can affect institutional environments by altering standards for accountability.

Executive succession can impart new knowledge and skills that make it possible to cope with the dramatic shifts in critical contingencies that follow regulatory punctuations. If current executives are not willing or able to pilot their organizations through the new competitive channels, organizations will search for new talent. Executive succession also has symbolic value, as it projects an aura of change in organizational direction. When uncertainty mounts, yesterday's leaders tend to be seen as having caused today's crisis, and their replacement symbolizes salvation and renewal.

Haveman et al. (2001) found that immediately following any regulatory punctuation, CEO succession rates will not rise. Instead, CEO succession rates will rise gradually as time passes. However, as might be expected, the regulatory punctuation did not increase the likelihood of outside succession.

Westphal and Khanna (2003) found that institutional investors have begun to advocate specific changes in corporate governance that are thought to protect the interests of shareholders but that threaten the interests of top managers. Thus, this is another kind of conflict and competition. The focus of institutional investors is on pressuring boards of directors to exercise independent control over management on shareholders' behalf. They advocate changes in board structure that will increase board independence from management, such as separating the CEO and board-chair position and creating independent nominating committees.

In the USA, it is not uncommon to have one person occupying the positions of chairperson and CEO. In many European and other nations, this combination is not allowed. The combination provides the CEO with greater possibilities for opportunistic behavior.

Institutional investors pressure boards to dismiss CEOs of underperforming organizations and repeal takeover defenses that were believed to protect managers from market discipline. Westphal and Khanna (2003) found that the common, underlying rationale for institutional investors demanding these changes is rooted in the agency conception of corporate governance, which suggests that boards must exercise discipline and control over management, because executives, if left to their own devices, will tend to pursue policies that benefit themselves at the expense of shareholders.

Flickinger et al. (2016) studied how CEOs protect themselves against dismissal. They addressed the question of why some CEOs stay in office during a performance downturn while others do not. Taking a social status perspective, the researchers argue that an individual's board network embeddedness—as reflected in the number of outside directorships—plays an important role in dismissal decisions. They predict that a high status of the CEO relative to the chairperson of the board protects an underperforming CEO against dismissal.

Flickinger et al. (2016) argue that a common way of capturing social status is by measuring the extent to which a CEO holds outside directorships, i.e., serves on the boards of other corporations. Outside directorships are a characteristic of the elite's social capital. Outside directorships benefit the CEO by increasing his/her monitoring experience. A CEO's outside directorships act as a source of status and intra-board power for the CEO. These status benefits of the current CEO may help to secure his/her position even in the case of poor organizational performance. A CEO's number of outside directorships is an important part of CEO power (Zhu and Chen 2015).

Westphal and Khanna (2003) studied how social processes by which the corporate elite may have resisted pressure from stakeholders to adopt changes in corporate governance that limit managerial autonomy. Senior managers and directors of large established organizations tend to possess a shared class-wide rationality or group consciousness as members of unified business elite. Members of this inner circle of business leaders are normatively expected to protect the interests of corporations and the executives who run them. A central interest is to protect the autonomy and final decision-making authority of top managers themselves. Boards are often a critical mechanism by which the solidarity of the corporate elite is maintained and the interests of corporate leaders are served. For example, it is not uncommon for corporate leaders to be present at each other's boards, where they meet each other in different roles: while one day a subordinate as the CEO, the other day a superior as member of the board. Boards provide a locus for socialization of directors who violate the priorities of corporate leaders who are not part of the system. While deviant behavior tends to be accepted by those who are inside the system, deviant behavior by executives outside the system is sanctioned.

Westphal and Khanna's (2003) findings suggest that control in corporate governance can be viewed as a social phenomenon. The corporate governance literature has drawn largely from economic perspectives such as agency theory, and in some cases micro-political perspectives, to explain the determinants of corporate control. These perspectives tend to assume that control lies with individuals or small groups, such as individual CEOs, boards, or owners, thus lending a somewhat atomistic and perhaps oversimplified perspective to theory and research on corporate control.

In contrast, Westphal and Kanna's (2003) study suggests how control can be exercised by the corporate elite as a larger social group. From a theoretical perspective, directors exercise social control over other directors not because it serves their own personal interests (whether economic or political), but because those directors violated normative expectations for members of the corporate elite by failing to respect the autonomy of managers on another board.

According to Westphal and Bednar (2005), CEOs often fail to initiate strategic changes in response to poor firm performance. Strategic persistence in response to poor performance results, in part, from a range of cognitive biases or perceptual distortions in executive decision-making. For example, CEOs have been shown to overattribute poor firm performance to uncontrollable or temporary conditions in the external environment and underattribute performance problems to the current corporate strategy. Executives fall prey to such attribution biases for a variety of reasons. They may become socialized into belief systems that take for granted the value of the current strategy. To the extent that they helped to formulate the strategy or previously endorsed the strategy, implicitly or explicitly, executives may be reluctant to acknowledge to themselves, colleagues, or external constituents that the strategy is not working. Moreover, there is evidence that executives tend to respond to poor performance by restricting their search for new information, ignoring information that reflects negatively on the current strategy, or engaging in a biased pattern of advice seeking that affirms their strategic assumptions and bolsters their confidence in the current strategy. They may also enter into a blame game, where they attribute weaknesses to everything else and everybody else (Eberly et al. 2011).

Outside directors may have social ties to the CEO or professional ties to the firm that make them reluctant to challenge the CEO's view about the viability of the current corporate strategy. Westphal and Bednar (2005) found that empirical evidence from the corporate governance literature does not consistently support this explanation, however. Although there is some evidence that boards comprising outsiders who lack social ties to management are more effective in controlling agency costs from overly generous executive compensation contracts, there is less evidence that directors' independence affects the likelihood of strategic persistence in response to poor performance or environmental change. Outside directors who lack social ties to the CEO or professional ties to the firm are necessarily not more likely to challenge top managers on strategic issues.

## CEO Compensation and Benefits

In 2005, the average US CEO's pay for 1 day was almost equivalent to the average worker's pay for 1 year. Since then, the salary gap between top and bottom in organizations has increased even further. In addition, a golden handshake by departure from the CEO position can trigger the payment of millions of dollars.

CEO severance has captured the attention of a wide array of audiences. A severance package is pay and benefits the top manager receives when the person leaves employment at the company. Ex ante severance agreements are frequently included as part of CEOs' initial employment contracts. These agreements guarantee an executive certain benefits in the event he/she is later dismissed by the board. The magnitude of severance packages for CEOs has created considerable controversy (Cowen et al. 2016).

Research has suggested that stock options and equity ownership have different motivational implications for executive risk taking. Certo et al. (2003) examined investors' reactions to the differing incentive properties of stock options and equity ownership in the context of firms undertaking initial public offerings (IPOs). They found that stock options and equity ownership interacted to influence the premiums that investors applied to IPO firms.

Executive stock options have the potential to significantly influence CEO ownership and firm ownership structure. McGuire and Matta (2003) examined the ownership and performance implications of the exercise of CEO stock options. They found that the exercise of stock options has no impact on the levels of CEO equity and no relationship with subsequent organizational performance. The decision to exercise stock options appeared to reflect risk-balancing concerns rather than expectations for future performance.

A central premise of agency theory is that organization can align the interests of chief executive officers and shareholders by designing compensation arrangements that reward CEOs for gains in shareholder value. Stock options are considered an effective alignment mechanism. However, as argued by Wowak et al. (2015), stock options can promote a lack of caution in CEOs that manifests in a higher incidence of product safety problems. They found evidence in regulated industries such as foods, pharmaceuticals, and medical devices. However, Bosse and Phillips (2016) emphasize that while standard agency theory logic suggests that paying CEOs with stock options will align their behaviors with the interests of the firm and result in higher firm performance, some empirical results show that this practice leads to more big losses than big gains.

The CEO can be viewed as a resource. The CEO as a resource might have superior or inferior management skills. Top managers of poorly performing organizations should think about voluntarily exiting because they do not represent valuable resources. A resource is something or someone that enable something to happen or not happen. Priem and Butler (2001) are skeptical of the CEO as a resource concept. They argue that there is no basis for discriminating among superior or inferior CEOs, other than waiting for performance results.

CEO compensation can influence the job of the CEO. Hall and Liedtka (2005) found that incentives created by CEO stock options and overall compensation significantly influence decisions to outsource information technology functions that are run by the CIO. The study provides evidence of a relationship between managerial self-interest and IT outsourcing.

Average CEO compensation has been high and steadily increasing over the period in which large-scale IT outsourcing has come into prominence. During 1992 through 2000 in the USA, for instance, the average value of the various components of CEO compensation grew from a total of $1.7 million to $8.5 million in large organizations (Hall and Liedtka 2005). Today, it seems that CEO compensation has tripled since 2000. CEO compensation plans tend to be quite elaborate, providing a variety of incentives such as annual bonuses, stock options, stock grants, and long-term incentive payouts.

IT outsourcing as a means to increase CEO compensation is interesting, since many companies regret this move and choose backsourcing after a number of years. However, when backsourcing occurs, the responsible CEO has long since left the organization. Thus, a short-term focus tends to be more profitable for a CEO than a long-term focus.

Hall and Liedtka (2005) found in their empirical study that CEO compensation appears to play a significant role in large-scale IT outsourcing decisions. The significant, positive coefficient reflects theory that, all else equal, stock option grants increase CEO willingness to make significant changes to firm structure. An important function of stock options is indeed to reduce the likelihood that CEOs will avoid beneficial changes to their organizations by increasing the convexity of the relationship between wealth and performance. Not all decisions motivated by options, however, are desirable from the shareholders' standpoint. Rather, high proportions of option-based compensation can create an incentive for CEOs to engage in low-value activities to destabilize the organization for short-term profits.

CEO compensation and benefits need to be at a level where the person is happy with it. At the same time, both investors and other shareholders would like to avoid overpay for CEOs. Underpay for CEOs, on the other hand, seems risky, since opportunistic behavior can be the result. There are several examples where hired CEOs considered their own pay to be below acceptable level compared to the wealth the CEOs contribute to create for owners. When observing how owners become richer and richer, some CEOs help increase their own compensation in illegal ways. An example is special projects, where CEOs alone handle money flows and let some of the money flow into their own bank accounts abroad.

Principal–agent theory focused on bounded self-interest suggests that CEOs, who perceive the treatment from boards as exceeding their expectations, can generate what Bosse and Phillips (2016) term agency benefits. Some CEOs exert exceptional effort when they perceive fair treatment that exceeds their expectations. Thus, boards can initiate positive reciprocity with a CEO that generates agency benefits. When the board and CEO are misaligned, then bounded self-interest will have negative consequences. On the other hand, when the CEO interacts with the board in ways that reinforce his/her expectations for justice, they affect social norms of justice. CEOs are socially influenced around the world. To the extent that expectations of fairness and justice are acknowledged and legitimated by influential parties, that pattern may have positive effects through society.

Agency theory explains how principals efficiently may organize exchanges with agents by employing mechanisms—incentive alignment and monitoring—in appropriate combinations. The challenge for principals is to realize the benefits of cooperation with agents while minimizing the sum of losses and achieving benefits as expected (Bosse and Phillips 2016).

Principal–agent theory explains the existence of large, elaborate CEO compensation contracts and underscores the potential for compensation to influence CEO decisions. The theory begins with the assumption that CEOs as agents are effort averse and seek to maximize personal utility rather than that of their organizations' owners as principals. To prevent CEOs from shirking or acting wastefully, owners can use compensation incentives that motivate CEOs to work harder and more responsible than they would otherwise by tying CEO wealth to organizational performance or owner wealth.

Consistent with this theory, empirical research finds strong evidence that CEO stock options and overall compensation balance drive a variety of accounting and finance choices. Further, the average relationship between compensation and CEO performance appears positive.

However, Hall and Liedtka (2005) found that not all CEO activities motivated by incentive compensation are in an organization's best interest. Noting that CEOs have private information and that perfect monitoring of CEO decisions is prohibitively costly (if not impossible); the principal–agent literature also argues that organizations must endure some residual risk that CEOs will act opportunistically. For instance, CEOs can make both real and accounting decisions that increase their personal welfare despite the fact that the decisions are not in their organizations' best interests. Given the dramatic increase in CEO compensation, the potential rewards of opportunism seem to have increased as well. Accounting scandals such as Enron have made the general public aware of the potential negative, almost irresistible compensation incentives contributed to the poor business decisions and ethical lapses that led to the collapse of Enron, WorldCom, and Tyco.

In the USA, the typical CEO is a white male. Only a few women and minority members are able to get through the glass ceiling into the CEO position. Hill et al. (2015) studied these few others compared to the dominant white males in terms of compensation. They found evidence that CEOs benefit from the value, rarity, and inimitability of their minority status such that they receive higher compensation relative to white males. The results for minority CEO compensation support economic arguments grounded in the resource-based view that value, rarity, and inimitability play a role in how CEOs are paid. The findings also challenge the hypothesis that minority CEOs receive lower compensation because of biases and stereotypes associated with minorities in the CEO position.

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