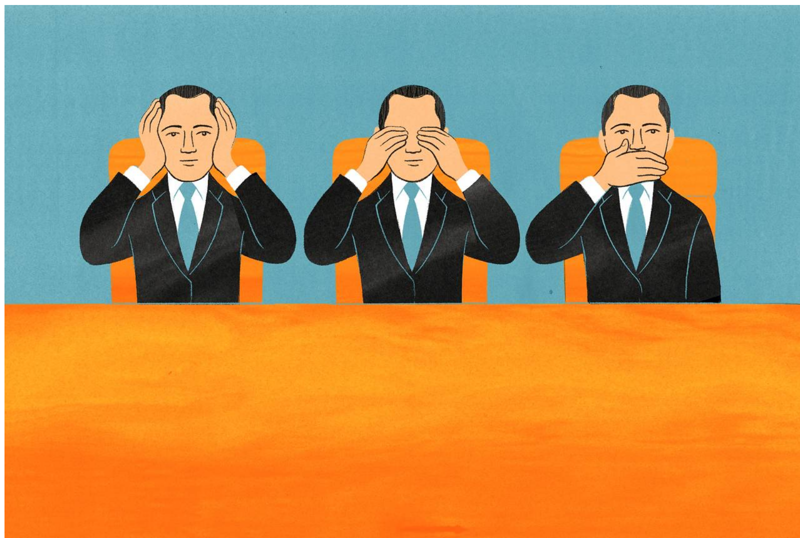
This copy is for your personal, non-commercial use only. To order presentation-ready copies for distribution to your colleagues, clients or customers visit https://www.djreprints.com.

https://www.wsj.com/articles/boards-may-have-a-hidden-bias-toward-the-ceos-they-chose-11576170708

JOURNAL REPORTS: LEADERSHIP

Boards May Have a Hidden Bias Toward the CEOs They Chose

If the directors picked the chief, they are less inclined to fire after poor performance, study says



People have a tendency to defend a choice even if it's clear they've made a bad decision. **PHOTO:** ALEX NABAUM

By Dave Ketchen and Jim Combs

Dec. 12, 2019 12:11 pm ET

Reforms such as Sarbanes-Oxley have improved corporate governance by preventing chief executive officers from stacking boards of directors with their friends and allies. But a more subtle bias still plagues many boardrooms—one that policy changes and legislation can't combat.

It's called choice-supportive bias—the tendency people have to defend a choice even if it is clear that they've made a bad decision, such as voting for a candidate who stumbles once elected or buying a car that later proves unreliable. The bias arises not from an intent to deceive but rather from an unconscious need to protect one's sense of self.

In a new study published in the Strategic Management Journal, we investigated whether choice-supportive bias affects corporate directors and, if so, what harm it does to companies. While the proverbial person in the street appears to be easy prey for choice-supportive bias, we theorized that directors' education and business experience might protect them.

JOURNAL REPORT

- Read more at WSJ.com/Leadership

MORE CEO COUNCIL

- The Challenges of a Changing Role for CEOs
- Keeping Your Talent Happy Enough to Stay
- Nancy Pelosi on Divisions Political and Economic
- William Barr on the Inspector General's Report

Unfortunately, that's not the case.

Remembering the positives

We started with an experiment where we asked 73 corporate directors to choose between two hypothetical CEO candidates. The candidates possessed comparable strengths (e.g., a great industry reputation) and weaknesses (e.g., viewed as a narcissist by some peers). After expressing a preference, directors were told that their favored candidate had in fact been selected to be the new CEO.

When later asked to recall each of the candidates' strengths and weaknesses, the directors tended to remember their chosen candidate's strengths and the other candidate's weaknesses, and they tended to forget *their* candidate's weaknesses and the other's strengths. The directors also attributed strengths to their chosen candidate and weaknesses to the other that weren't part of the original description of either candidate. Despite their business acumen, the directors unintentionally rearranged the facts in their minds to support their choice.

Having established that corporate directors are susceptible to developing faulty perceptions of their choices, we then asked: Does choice-supportive bias have financial implications? Directors who helped hire the CEO might support the incumbent more than the company's performance warrants.

The possibility of this bias playing out in the boardroom is most worrisome when a company is on shaky ground, so we examined data from poorly performing S&P 1500 firms across 10 years. We found that directors who helped choose a CEO were unusually reluctant to replace that executive. Put another way, the more directors on the board were involved in the CEO choice, the lower the chance that a CEO would be fired in the year after two consecutive years of underperformance. Such directors also tended to overpay the CEO relative to his or her peers despite poor performance.

Positive change

One implication is that some board turnover after hiring a new CEO is healthy. There's no guarantee, but on average, our data on poorly performing firms indicate that replacing just one of the directors who helped hire the CEO increases the chances of removing the CEO by about 20% within the year following two years of poor performance.

Another implication is that choice-supportive bias has a smaller impact on board decisions if a board has highly experienced directors among its ranks, as measured by experience on other boards. Thus, when turnover happens, filling vacancies with highly experienced directors is wise.

In addition, we suspect that directors' susceptibility to choice-supportive bias has implications for other high-stakes decisions. For example, directors might be more reluctant to undo failing acquisitions and international expansions if those moves took place under their watch.

If so, awareness may be half of the battle. As is true of most psychological biases, simply being alert to the possibility of choice-supportive bias distorting perceptions can help directors protect against its effects. Understanding that it is natural to view one's decisions too favorably can lead directors to ask harder questions if those decisions are delivering poor outcomes.

Dr. Ketchen is the Harbert Eminent Scholar at Auburn University and Dr. Combs is the Della Phillips Martha Schenck Chair of American Private Enterprise at the University of Central Florida. Michelle Zorn, an associate professor of management at Auburn University, and Kaitlyn DeGhetto, an assistant professor of management at the University of Dayton, also contributed to this article. The authors can be reached at reports@wsj.com.

- **College Rankings**
- **College Rankings Highlights**
- **Energy**
- **Funds/ETFs**
- **Health Care**
- **Leadership**
- **Retirement**
- **Small Business**
- **Technology**
- **Wealth Management**

Copyright © 2019 Dow Jones & Company, Inc. All Rights Reserved

This copy is for your personal, non-commercial use only. To order presentation-ready copies for distribution to your colleagues, clients or customers visit https://www.djreprints.com.