

## **Finding the right Non-Executive Directors – article written for the 2012 AIM Guide**

Chris Spencer-Phillips, MD of First Flight summarises the important aspects to be considered when appointing Non-Execs and the role that they should play in the development of UK businesses.

### **1. Introduction**

The Walker Report on UK banks and the financial sector established clear links between board behavioural deficiencies and poor business performance. The report has repercussions beyond the financial sector and has resulted in a revised UK Corporate Governance Code which now includes a greater focus on board behaviour, new principles on the role of the Chairman and Non-Executive Directors and new provisions on the frequency of board evaluations and Directors development reviews.

Some provisions are as follows:

- Provision B.1.2: "Except for small companies, at least half the Board, excluding the Chairman, should comprise Non-Executive Directors...a smaller company should have a least 2 Non-Execs."
- B.2.4: "An explanation should be given if neither an external search company nor open advertising has been used in the appointment of a Chairman or Non-Exec."
- B.2: "There should be a formal, rigorous and transparent procedure for the appointment of new Directors (including Non Execs) to the board."
- B.2: "The search for board candidates should be conducted, and appointments made, on merit, against objective criteria and with due regard for the benefits of diversity on the board, including gender."
- A.3.2: "Non-Executive Directors should undertake that they will have sufficient time to meet what is expected of them."
- A.4: "Non-Executive Directors should constructively challenge and help develop proposals on strategy. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible."

The "comply or explain" Code is an excellent document to "facilitate effective, entrepreneurial and prudent management that can deliver the long-term success of the company"; it also encourages companies to appoint Non Execs who can add real value but are they achieving this?

### **2. What benefits do Non-Executive Directors bring?**

- Outside objectivity
- Constructively challenge the company's strategy and major decisions to ensure the company is doing the right things
- Review plans and budgets that will be used to implement policy and strategy
- Be a confidential sounding board for the MD/CEO (mentor) and maintain the focus of the MD/CEO
- Have the experience to objectively assess the company's performance
- Ensure good Corporate Governance and best practise
- Provide outside experience of the workings of other companies and industries
- Bring contacts
- Possess the tact and skill to work with the Executive Directors, providing support and encouragement where difficult decisions are being made & ensure that they are acting in an appropriate manner
- Provide comfort to company's suppliers, bankers, funders and other stakeholders.
- Increase the competitiveness of the business.

### 3. Who is the right Non-Executive Director?

- A company's Board should set the strategic aims and direction and ensure that the necessary financial and human resources are in place for the company to meet its objectives. In order to achieve this, the balance of the board has to be right in terms of skills, experience and personal styles.
- Corporate Governance guidelines recommend that Non Execs should outnumber the Executives on the Board and adding appropriate Non Execs provides the greatest scope for getting the right balance of skills and personalities on a Board. In order to be able to introduce the right Non Exec first requires an understanding of the skills and personalities that already exist on the Board.
- Balanced Boards should have 4 different skills in order to operate effectively covering each of these core areas:
  - ✚ strategy (the big picture) - operations (the detail)
  - ✚ drive (the accelerator) - monitoring Risk/Governance (the brake)Effective Boards strike a balance between competing polarities such as being entrepreneurial but with sound risk management.
- Every Board also needs the right balance of types or categories of people to operate effectively and one of the simplest ways to categorise people was developed by David Kolb who categorised people in four ways: activist, pragmatist, theorist and reflector. The differences between the four categories can be illustrated by how they would learn to ride a bike:
  - ✚ The activist will get on the bike and try to ride it
  - ✚ The pragmatist will watch someone else ride it and then try
  - ✚ The theorist will look at the principles behind riding a bike
  - ✚ The reflector will think about why they might want to ride a bikeA balanced Board has a mix of all four skills and all four types of people. First Flight likes to understand the current balance of the Board of its clients in terms of skills, diversity and personalities so that we can make sure that the addition of an incoming Non Exec will enable the Board to operate effectively and "the whole being greater than the sum of the parts".
- There is a temptation to appoint Non Execs who are "a safe pair of hands", "won't rock the boat" or "will look good on the letterhead"; sadly we still see examples of the use of the 'old-boy network' or cronyism (as Sir Derek Higgs called it) in sourcing Non Execs. Appointing Non Execs in such a way goes against the very essence of what Non Execs should be (independent) and is likely to prevent the Board from operating effectively.
- Many companies appoint "generic Non Execs" who often have multiple roles. The Walker report recommended that to be effective Non Execs shouldn't have more than five roles. First Flight is strongly in favour of this and also providing Non Execs who are "live" and often still in executive roles elsewhere therefore having a better sense of where the mousetraps are; with things in business moving so fast this is helpful if the Non Exec is going to add real value to a business and if they don't why are they there?
- Boards should also have a diversity of members enabling them to represent and understand their stakeholders; 85% of products and services in the UK are bought by women so it makes sense that more of them are on Boards. Diversity is not just an end in itself; it is a very powerful way of getting the balance of the Board right.
- First Flight is a strong advocate of broadening the Non Exec gene pool as well as placing Non Execs who balance the skills and abilities in the Boardroom and add real value.

### 4. What does an AIM company typically pay a Non-Exec?

- The average time commitment for a Chairman has increased since the Walker report to 36-40 days pa, which increases for larger companies due to the number of sub-committees such as Audit, Nomination, Remuneration, Risk and Strategy committees.
- The average time commitment for a Non-Exec is 24-30 days pa, again increasing for larger companies.
- Board meetings, including preparation, tend to take up about 40% of the time, with strategy and planning meetings taking 10% & sub-committees 20%.

- The average pay for the Chair of AIM-listed companies is between £1,200 & £1,700 per day for smaller companies (£40k pa) and £2,000 to £3,000 for larger companies (£100k pa).
- The average pay for a Non-Exec in an AIM-listed company is around £1,300 a day for smaller companies (£25k pa) and £1,800 a day for larger companies (£50k pa).
- 15% of Chairmen and 10% of Non-Execs receive part of their fees in shares.
- The prevalence of share options in AIM-listed companies is high with around half of Non-Execs benefitting.

## **5. What should a company pay to recruit a Non Exec?**

- City & West End search firms charge iro £40-£60k for providing a Chair or Non-Exec; to justify these fees they have expensive offices and large research departments but neither of these are now needed to provide an effective service.
- Most companies below the FTSE 350 cannot afford such fees and are forced to resort to the 'old-boy network' or cronyism as explained above which does not provide transparency, choice or even the right Non Execs and is an unacceptable way of recruiting Non-Execs today.
- The big Search firms tend to work within a 'small gene pool' with the same Non-Execs appearing on multiple boards which is why they have got into a mess with diversity.

## **6. The options for AIM companies looking for a choice of effective Non-Execs**

- First Flight is focused solely on providing Chairs and Non-Executive Directors with the largest Non-Exec database in the UK.
- We have successfully completed 125 Non-Exec projects.
- In addition to providing non investing Non Execs we pioneered the concept of investing Non-Execs with over £5 million invested to date by our Non-Execs.
- First Flight's success comes from its substantial, up-to-date database (over 5,400 Non-Execs – selected from 35,000 CVs, so only one in seven goes onto our database), providing fresh talent drawn from a variety of sectors (most having been Non-Execs before), supported by discreet search and focused advertising (at our cost) enabling appropriate candidates to be identified within three weeks.
- First flight's clients therefore enjoy the benefits of a fast and specialised service with competitive fees half what the big Search firms charge but most importantly providing the right Non Execs who can add real value.

### **Chris Spencer-Phillips, Managing Director of First Flight**

Email: [chris@ffplacements.co.uk](mailto:chris@ffplacements.co.uk)

**First Flight is a specialist Non-Executive Director resource; "this is all we do and we do it well".**

[www.NonExecutiveDirector.co.uk](http://www.NonExecutiveDirector.co.uk)

First Flight is sponsor of the Non-Executive Director of the Year award at the Quoted Company Awards 2010 & 2011.

Some information in this article is taken from First Flight's Survey of Non-Executive Directors in Unquoted, AIM & PLUS Companies.

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