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## *A good piece of advice*

HOW YOU CAN USE NON-EXECUTIVES TO UNLOCK VALUE IN YOUR BUSINESS



# INTRODUCTION BY DYLAN WILLIAMS



The growth journey for any business is obviously something of great interest to Coutts as a Wealth Manager.

Many of our 20,000 clients who are entrepreneurs or business owners have followed that journey and now have valuable insights around their experiences.

In “The long goodbye” report we looked at expectations around the experience of exiting the business. This time we have turned our attention to an earlier stage of the journey when new skills need to be brought to bear to support the growth plan.

There is no doubt that the ability to create strong effective teams is a key attribute for entrepreneurs at this stage and many look to the appointment of non-executive directors and advisers as part of their strategy for this.

This report seeks to distil some of the experiences of a number of our clients both in using non-execs in their businesses and also from the perspective of being a non-exec.

The aim is to provide valuable insight that is particularly focused towards the SME marketplace rather than the listed company sector where most of the focus on this topic lies. I hope that it will stimulate thought and in a modest way enhance the prospects for growth and add value to businesses.

Dylan Williams | *Managing Director, Coutts*





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## EXECUTIVE SUMMARY

Taking on your first non-executive director can be the first step on a long and possibly very mutually rewarding journey.

But in every case it is a big step. In the first instance, many companies feel they need the expertise of an outsider but don't know whether a non-executive director or a business adviser offers the best way forward. Once the decision is made to go down the non-executive route they face the challenge of recruiting the right person for the job and coming up with an appropriate way of rewarding them for their time. Further down the line, the original non-executives may have outlived their usefulness, creating a requirement for fresh blood to meet the demands of new circumstances. If preparation is the key to execution then every entrepreneur going down this road must be clear about what he or she wants to achieve at each point of the journey.

Drawing on the experience of non-executive directors and business owners, this report takes a comprehensive look at the experience of hiring and managing non-executive talent.

The key findings are:

- **Evaluating the role and looking at the alternatives.** The first step for any entrepreneur is to decide whether they need a non-executive director or a business adviser. Taking on a non-executive isn't the only option or the right option for a business that wants to unlock more value as it grows. In some cases an adviser may be a more suitable option and our survey shows that businesses benefit the most when they make a distinction between the roles of adviser, non-executive director and non-executive chairman
- **Getting the skills required.** Not all non-execs are the same. Although 57% of those we spoke to said a broad commercial career experience was a pre-requisite for the role, this needs to be balanced with specific skills around starting and selling a business, raising finance or selling a business as part of a management team. Looking at the balance of the CV is key in getting the right person for the job
- **Sourcing the right person.** Although just over half (55%) of entrepreneurs say they would use recruitment agencies to source the non-exec for their businesses, business referrals are the selection route of choice for 88% - and the preferred route of approach by non-execs themselves
- **Getting the balance right.** A significant minority (16%) of business owners are concerned that the recruitment pool is too narrow and feel there aren't enough women on boards, but see the right match of person to the job in hand as best for their business rather than positive discrimination
- **A question of trust.** Businesses are concerned about the risk of hiring a poorly performing non-exec. For their part, non-executive directors say they would only be prepared to take up positions if they felt they could work with the board and make a difference. Executives may have to woo good non-executives
- **Pay and reward.** Non-execs and entrepreneurs don't see eye-to-eye on how they should be paid for their work. No entrepreneur we spoke to favoured payment in shares alone as the way to remunerate non-executives. In contrast 10% of non-execs favour this form of payment. Mix and match is the order of the day and both sides need to negotiate to get what they want
- **Keeping it fresh.** Over half of entrepreneurs (55%) and a third of non-executive directors (35%) feel that non-executive contracts should be limited. There is broad agreement that NED teams should be refreshed and that individuals should not remain on the board when they cease to add value

These are the views taken from a panel of over 50 leading UK entrepreneurs and non-execs which have been distilled into this report to provide insight and practical advice for any business thinking of appointing a non-executive.

## | 01 | WHAT A NON-EXEC MEANS FOR YOUR BUSINESS

The work of non-executive directors (NEDs) seldom makes headlines. Even when it does it tends to focus on those in larger business who have fully fledged members of the board – with all the associated legal responsibilities - and a remit to influence and guide rather than execute managerial decisions. In the boardroom pantheon they stand in the often substantial shadow of the executive team.

So it can seem to outsiders. Yet within the closed confines of the boardroom, a good non-executive director not only wields considerable influence but can also be a catalyst for the changes needed to take a company forward.

That might be a former FD taking a non-executive role to help a growing business raise finance, or an experienced entrepreneur working with a start-up CEO to build the right management team. These activities have a clear output but sometimes the benefits aren't quite so easy to quantify. In some cases the most valuable role played by a non-executive director might well be to act as a sounding board for a young MD who has plenty of ideas but not necessarily the confidence or experience to carry them through.

Whatever the role, the NED is there to draw on his or her business experience. That sounds straightforward enough but the relationship between a non-executive and the board he or she serves on isn't always easy. Unless both company and NED are very clear about the purpose and parameters, the position occupied by the non-executive can be, to say the least, amorphous.

It's perhaps indicative of the ambiguity surrounding the role of NEDs that back in the early 2000s – in the wake of the Enron scandal - Derek Higgs spent many months preparing an addition to the Combined Code of Corporate Governance that set out the role and responsibilities of non-executives in a huge amount of detail.

Sadly the Higgs's Report focused on companies with shares trading on the London Stock Exchange main list and had little relevance to small and medium sized, privately owned companies. In the rarefied world of the LSE, a major function of non-executive directors is to represent the interests of a broad shareholder base and act as a cornerstone of corporate governance.

In the case of a small or medium sized entrepreneurial businesses the role is usually focused on being an agent of growth and transformation. In fact, apart from bringing an independent perspective, the role of a NED in businesses like these bears little relation to its larger cousins. The non-executive director is in fact more of a non-executive adviser.

And with a cost associated to the investment in this resource, any business thinking of hiring a non-executive adviser of this kind, must answer some fundamental questions. What will this person bring to the business? How can we measure their contribution? Could that value be added more effectively by someone – such as an adviser or interim FD – in a different role?

If answering these questions is key to getting the right person then understanding the journey you will go on with them and the expectations on both sides is critical. The most obvious starting point is defining the non-exec role itself – which starts with the needs of the business.



## | 02 | DEFINING THE NEEDS OF THE BUSINESS

At the most basic level, a non-executive director can provide an extremely cost-effective means of plugging gaps in the boardroom team. Working for perhaps one or two days a month, a non-exec director won't add excessively to the wage bill but can bring to bear expertise and insight that would otherwise be unavailable. Paul Franks, an investor at Gresham Private Equity, puts it simply: "The role of a non-executive comes down to what is needed in the business – whether it is guidance, access to people or someone with the skills to build it up."

In that respect, the appointment of a non-executive is best linked to a particular goal. For instance, a company seeking to break into a new market may hire a NED with appropriate contacts or trading

experience. Similarly, a business planning to raise funds from private equity or through flotation will often appoint a non-exec with City connections.

Sometimes the role can be more fundamental.

Deborah Leary is chief executive of Forensic Pathways. She says one of the key benefits of a non-exec director is the presence of someone who can bring the perspective of an outsider to the board where executive members are all too often caught up in the detail of day-to-day management and find it difficult to see the bigger strategic picture. "To me the key is bringing clarity to what the business needs. That's something we don't get in the day-to-day."

The importance of this strategic role is borne out more widely by the panel of entrepreneurs who we surveyed for this report. When we asked them what the key criteria was for judging the suitability of a non-executive director to fulfil a role, they cited strategic strength (73%) at the top of the list just behind track record (89%). The implication here is that it is the ability of non-executives to leverage previous experience and inform the strategic decision making process that is highly prized.

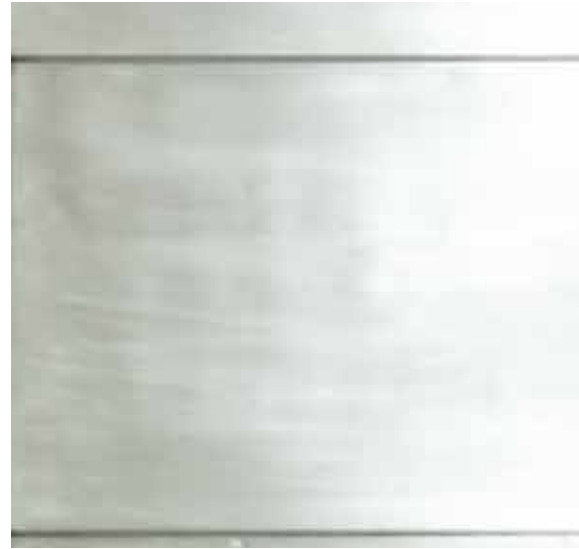
Non-executive directors themselves who we interviewed also put a high premium on their strategic input. When asked about key criteria that businesses should use to judge the quality of their NEDs, 83% say it is strategic strength.

### THE NON-EXEC PERSPECTIVE - COMMITMENT IS KEY



**Having sold the website [trustedreviews.com](http://trustedreviews.com) and [bit-tech.net](http://bit-tech.net), Hugh Chappell is an entrepreneur turned non-executive adviser to a number of publishing and online businesses.**

"A simple question for me when considering non-exec roles is what added value I can bring to the table and what is actually required. When I owned my online publishing businesses I did not hire any non-execs. I came across several who were offering their services however all were from print publishing backgrounds. I was unable to see how they could add value. I am a non-exec for [MyVouchercodes.co.uk](http://MyVouchercodes.co.uk), a fast growing and highly successful business. The owner is dynamic yet still young and the business has grown rapidly so with my knowledge of management, strategy, risk and people, we realised that the one plus one would equal three: we are more than the sum of the parts. My experience is that if owners or senior management genuinely want independent advice then it will work. To establish this, it is important to meet the entire team. I have considered non-exec roles where having sat down with the management team around the table I have walked away. Time is also an area where both parties need to be realistic. In my experience 'one day per month' often means more. If you are a committed person it is impossible to walk away simply because the 'meter' has expired."



## | 03 | NON-EXEC DIRECTOR OR NON-EXEC ADVISER?

Non-executive directors are not the only option for businesses seeking guidance and technical expertise – an adviser, consultant, or in some cases a bank manager can offer similar benefits. It all depends on which stage in the growth cycle you are and what the objective is.

This is something that business owners recognise: when it comes to sourcing external help it's often a question of horses for courses. For instance, when we asked our panel of entrepreneurs who was most suited to the role of raising finance or planning a public listing, more than half (55%) say they favour an adviser rather than a non-exec-director (15%) or non-executive chairman (27%).

But when it came to providing strategic input and testing current thinking in the management team, respondents clearly favour non-exec directors (61%) over advisers (22%).

The survey results also indicate a distinct role for non-executive chairmen. For instance, when asked who was the best person to help define strategy, 44% of business owners say the non-executive chairman, against a 33% response for NEDs and none opting for advisers. The chairman is also favoured over the alternatives for the roles of stakeholder management and developing exit strategy. However this may be a role which is only understood and appropriate for larger businesses who can afford a dedicated person in this role.

While the job description is one thing to consider, so too are the dynamics and the relationship between your non-exec and the business.

The ability of one or other party to deliver on a clearly defined set of goals is important but not the only priority. There are also relationship issues to



consider. The interaction between a NED and the board will be very different from the adviser/company relationship in a number of ways.

For instance, as Andrew Morris, Chief Executive of the Academy for Chief Executives, points out, advisers are often more project-focused and can be much more focused on delivering transformation quickly:

“An adviser has more teeth. As NED you are part of the furniture. An adviser brings about change in a short amount of time.”

It is also the case that many owners in growth businesses prefer the goal-oriented approach of an adviser to the broader strategic input and willingness to challenge perceptions and assumptions that a non-executive director brings to the party.

However, circumstances and dynamics change. Deborah Leary says

it is possible for businesses to look ahead to a time when it will be right to augment the boardroom team with non-executive talent, even if present circumstances dictate a different solution. “We are starting with advisers and moving to non-execs.” she said.

The way the non-exec is expected to weigh with the CEO and the rest of the management is also critical.

Andrew Morris says the effectiveness of a non-executive may be limited if the CEO – and, by extension other senior managers, are wary of them.

“A troubled CEO may be much less open with an NED. As a non-executive you are part of the power base and senior members of the management team may not want to share the issues that matter.”

This kind of situation will clearly be frustrating for the NED and also

wasteful in terms of the resources available to the company.

The message is that business owners should assess their requirements not just in terms of the skills and track record of potential non-executive directors and advisers, but also through the viewpoint of the company’s existing management dynamics. It may be that a business may not be ready for the non-executive director and in such cases an adviser would be more appropriate.

**THE BUSINESS PERSPECTIVE - MOVING FROM ADVISERS TO NON-EXEC**



**Deborah Leary is Chief Executive of Forensic Pathways and is developing the way she works with non-execs in her business.**

“We are at the stage where we could benefit from a non-exec. One aspect of it is whether we find someone who can open doors or whether they have a sharp business focus. The key for me is bringing clarity to what the business needs which you don’t get if you are in there day-to-day. We are starting with advisers and moving to non-execs. We are creating an advisory board as a first step before deciding how we move forward and what we need. They are working on special projects and some are working in the business. We had used subject matter experts in the past but discovered that they lacked business expertise.”

| 04 | **LOCATING YOUR NON-EXEC**

Despite the apparent strong match between the skills desired by entrepreneurs and those on offer, finding the right non-executive director can be challenging – a key issue raised by our research.

Hugh Chappell is an entrepreneur who has sold a number of businesses and is currently an active non-executive adviser. He says when he was growing his original businesses he was unable to find a non-executive director who could genuinely contribute because of a simple lack of relevant current industry experience.

So where do you go for the right people? Of our panel of entrepreneurs, 55% of business owners cited recruitment agencies and head-hunters while just 6% said they would resort to advertising. Networking was clearly the most favoured recruitment channel with 89% saying they would use this route.

On the face of it, sourcing a NED through a recruitment agency seems the simplest option – if only because it outsources much of the work. However, those who have experience of the recruitment process highlighted the potential pitfalls. Key issues were the limited ability of recruiters to match the right non-exec to the right business and the time intensity of sorting the quality candidates from Directorbank – which has 10,000 or so directors on its books.

Referrals then are key and the best way to find the right people is through networking. Bridget Blow is a former chief executive in the IT industry and a Non-Executive Director for Coventry Building Society, Birmingham Hippodrome and consumer electronics firm Alba. She says that the most successful non-executive appointments are often

those you know or those that are drawn from your network.

Of course, the ‘network’ is an ever-changing beast and over time any business will come into contact with talented people who could conceivably make a positive difference if employed in a non-executive role. But according to Gresham’s Paul Franks, businesses must be clear about their own objectives. “Networking is the key, but you need to be clear about what you want,” he says. “For instance, it might be difficult to match up the needs of the MD – which will normally be about getting more customers with the interests of a chairman, which will be the application of commercial business expertise.”

## | 05 | PLANNING FOR PERFORMANCE

Regardless of how shortlisted candidates are selected, there is always concern that a newly appointed non-executive director – even one with an exemplary track record – simply won't deliver benefits. Although 44% were confident of getting good performance from their NEDs, 33% of our entrepreneur panel said they had experience of poorly performing NEDs.

There are no doubt some negative pre-conceptions – not least the stereotype of the time serving old hand who is mainly concerned with adding value to his CV rather than enhancing the boardroom fire power of the companies he serves. As Andrew Morris puts it: “One concern is the stereotype guy who tends to come in without reading the papers.”

It's certainly the case that a significant number of NEDs have a CV of businesses that runs into

double figures. When we asked the non-executives in our survey how many companies they advised 31% were in the 5-20 category, with 10% recording 10-15. In contrast, just 2% were advisers to just one company. The survey didn't ask about the current size of the portfolio, so a NED with 15 companies on his CV isn't necessarily working with that number of businesses at any one time.

Nevertheless, while executive teams value the experience of their NEDs, the size of the current, active portfolio should be taken into consideration. A hiring company will want to be assured that the incoming NED will have sufficient time to fulfil their obligations.

### **Relationships matter**

A key part of performance is the personality and fit with the business. Non-executive directors occupy a

curious position in that they are part of the team and yet separate from it. As team players it's important to fit into the culture and work well with the executive team. Certainly, our entrepreneur panel places a high premium on the relationship not just with the CEO but the wider team with 73% saying good chemistry between non-executive and management team was essential, as did a similar percentage of NEDs.

On the other hand, a big part of their role is to challenge the assumptions and strategies of the executive players. As Andrew Morris observes: “You (the NED) are there to do something such as change the behaviour of the board. That requires a balance of sympathy and challenge.”

And as William Wells, former CEO of Chestertons who holds a wide variety of non-exec roles says, that can be a tricky act to pull off. “A non-exec must

### **A QUESTION OF CULTURE – AND SIZE**

**David Soskin is an internet entrepreneur who was CEO of Cheapflights until 2008 and is now an adviser to two online businesses [mysupermarket.co.uk](http://mysupermarket.co.uk) and [swapitshop.com](http://swapitshop.com).**

“Whether it is a non-exec or an adviser they must be sympathetic to the culture of the business. The best NED with the best CV may not be the right person. This overrides the skill base or industrial knowledge. Culture is critical because sympathy to the culture is key to being able to challenge. For an early stage entrepreneur looking for an adviser, the question to ask is: ‘what are the strategic levers you need to pull to make a difference and what am I lacking’. Ask that challenging question and fill in the gap with a non-exec. And remember the role of corporate governance carried out by NEDs depends on the size of business. For a small business, this is less complex. If you are looking for a flotation then this component does become much more difficult and important.”

challenge. If they are too close to the culture of the company, they won't be able to do that," he said.

On the other hand, too much challenge – or lack of sensitivity about the dynamics and values of the business – can also be counterproductive, a point made by David Dey, a former BT board member and serial NED in the telecoms sector: "A non-executive adviser must be sympathetic to the business," he says. "The best NED with the best CV may not be the right person for the business. Culture is critical."

The executive team also has a balancing act to perform. A prerequisite of the hiring of a board member is that they will be able to work with the other board members, so a good relationship is important. The question is the degree to which the executive team will welcome challenge as part of that working relationship. If not, there are some real question marks as to whether the appointment will be successful.

### **More than a day job**

Another key issue in getting the right level of value and performance from your non-exec is making sure they want to do the job and work with your business.

When asked about their motivation in taking up non-executive positions, 65% said it was because they enjoyed the strategic challenge, 51% cited the opportunity to apply skills learned in previous roles and 42% pointed to a passion for growing businesses. The results suggest that non-executive directors are highly motivated people who are keen to make a difference.

The corollary is that before taking up a position, a good non-executive will want to be assured that it will be possible to make a positive impact. In other words, if the hiring company is looking for a good fit, so is the non-executive candidate.

That was a point made very forcefully by the non-executives we spoke to. Kevin Riches says companies will often have to 'woo' potential non-executive candidates while William

Wells spoke of the NED's need to do due diligence on the company they want to work for before taking up a post.

Equally important, many of the non-executives we spoke to made it quite clear they would be prepared to walk rather than accept a position where the personalities involved or the circumstances would make it difficult to add value. Paul Franks put it succinctly: "Good non-executives say no to most opportunities."

### THE IMPORTANCE OF THE RIGHT RELATIONSHIP

**Mark Hales is an entrepreneur with experience ranging from the mentoring start-ups to angel investment.**

“For me getting advice isn’t about going for a non-exec. It starts with mentoring where you build a relationship and it goes from there. It is wrong to think you need a board of non-exec from the start. In the same way you get turnaround experts you need the same sort of specialist expertise in a business as it grows. That may be someone who is good at bringing a concept to market, someone who can build a team, someone who can bring stability or someone who can find a buyer. If you do have a non-exec, one problem that can arise is around delivery when a non-exec gets into role, particularly at the smaller end of the market. It is almost like you need a training course for working with non-exec. I have met non-exec who just want to fill as many days as possible – they are the ones you don’t need. To attract the right people you need to sell the business because the people you really want are the ones who don’t need to do it.”

### FOCUSING ON MAKING A DIFFERENCE

**Andrew Morris is Chief Executive of The Academy for Chief Executives, he believes the focus for any non-exec arrangement must be focusing on a specific issue.**

“From my perspective there seem to be some clear reasons that you would get a non-exec: to deliver growth, to work towards an exit, to cover a skills gap, to sort out governance issues or to address a crisis. In many instances after an initial period the question arises as to what difference an NED is making so the formal appointment of a non-executive director may not be the solution to your problems. You must be particularly careful if it is a tough time for the business. A troubled CEO will be less open with a NED but with an adviser it could be different. You have to remember that a non-exec is part of the power base of the business and a senior member of the management team will not necessarily share the issues that matter.”



## | 06 | DELIVERING VALUE FROM THE RELATIONSHIP

A good non-exec will work hard for your business and of course, all that investment will require a reward. But what is the best way of rewarding your non-exec and what do they expect?

When asked their preferred method of remuneration, 10% of our NEDs say shares in the business, 23% named a flat fee and 66% opted for a mixture of the above as a way of being paid for their services (with share options drawing a zero score).

Our entrepreneur panel took a different view with no one at all favouring the shares in the business alone, 36% preferring a flat fee and 5% naming share options. 58% said a mixture of the two were best.

While the 'mixture of above' responses indicate that executives

and business owners favour negotiation and flexibility when deciding on the final package, the results suggest a divergence of interest and the need to be clear about what you are prepared to trade for the right advice. The other part of the bargain will be the scope and length of the non-exec engagement. Circumstances change. When a company is relatively young the role of the non-exec is likely to be focused on providing the experience and market expertise that will enable the business to grow more quickly.

At a later stage, the requirement may well be for a non-executive director with the City or financial sector contacts to help the business raise the finance it needs through private equity or flotation. And once the





business has a broader base of shareholders, the issue of corporate governance comes to the fore.

The upshot is that a non-executive director is not forever. As the business develops there will be a need to hire new talent and dispense with those whose services are no longer essential.

Our research found that 35% of NEDs and 55% of business owners felt there should be a time limit on non-executive contracts.

When we probed this in more depth, our panel of non-execs and entrepreneurs agreed that whether it was a fixed term appointment or an agreement which was reviewed yearly it was critical – in the best interest of the both non-execs and the business itself – that some sort of review

mechanism is built into a non-exec arrangements from the outset.

Ultimately the decision on whether or not to retain a NED should be based on the value they add at any given time and as the business develops the role of the existing non-executive team should be constantly assessed.

### **Methodology**

The contents of this report are based on research conducted on behalf of Coutts by Native Consultancy.

The research consisted of three phases:

- Qualitative research from focus group discussions among entrepreneurs and businesses who had experience of non-execs
- Quantitative research from a randomly selected sample of entrepreneurs consisting of over 200 respondents
- In-depth interviews with individuals with direct experience of business advisers based on the findings of the research

The research was completed in September 2011.



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