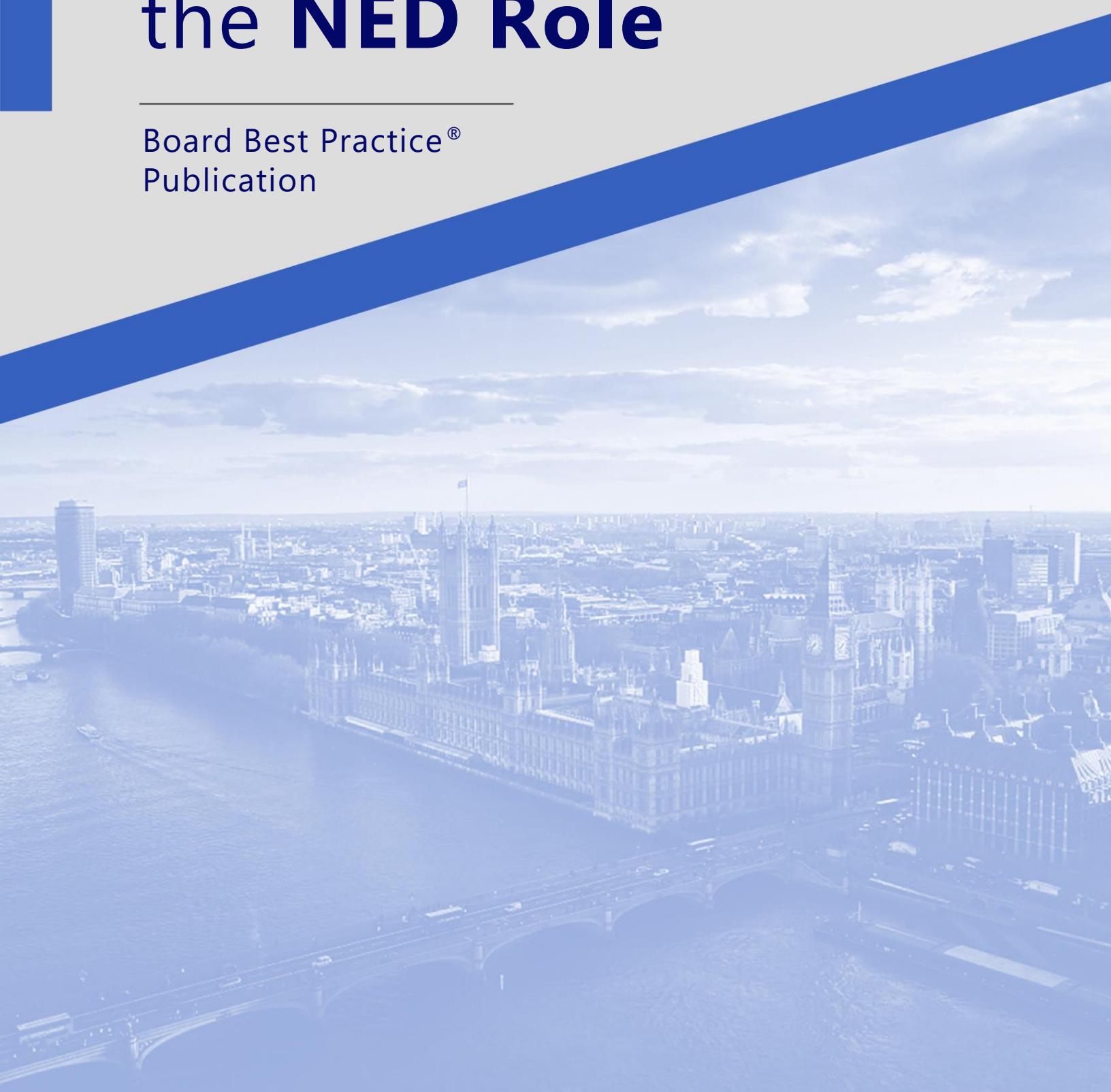


What to Expect of the NED Role

Board Best Practice®
Publication



Preface

In consultation with the NEDonBoard community, this document has been created by NEDonBoard for the information of non-executive directors (NEDs) and organisations considering appointing NEDs. It aims to identify common features of the NED role across different sectors and types of organisation in the UK.

NEDonBoard is the professional body for non-executive directors and board members in the UK. It is an independent membership organisation, focused on delivering value to its members.

NEDonBoard delivers value in a number of ways:

- It informs, connects with and represents the non-executive director and board member community.
- It upholds the highest standards of professionalism, governance and ethics.
- It promotes the effective operation of boards. It does this by facilitating among individual board members and those aspiring to board roles better awareness of the work of boards and directors and the responsibilities that attach to such work.

This document is freely available. It is not tied to, or influenced by, the agenda of any outside organisation. Further reference material is provided in the appendix.

We do hope that you will find this guide useful and that it will support you.

Jean-Philippe Perraud, General Director of NEDonBoard



Important disclaimer

This document discusses the nature of directors' duties within the context of the UK legal and regulatory framework, but it should not be relied upon as an exhaustive guide to a NED's legal responsibilities. It is the responsibility of every NED individually to understand and abide by the regulatory and legal requirements of their role.

To improve your understanding of NED legal duties, responsibilities and liabilities, please contact team@nedonboard.com.

NEDonBoard runs dedicated courses which it designs for those looking to start a NED career or those in need of a refresher.

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Initially published in June 2017, this NEDonBoard Board Best Practice® guide was edited in March 2019 by **Mark Cardale, Charlotte Morgan and Elise Perraud**. Elise Perraud is the NEDonBoard Chief Operations Officer. In addition to her role at NEDonBoard, Elise provides risk management, risk governance, assurance and corporate governance consultancy advice to financial services clients.

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Introduction

There is growing awareness of the NED role and a growing number of organisations are appointing NEDs to improve the effectiveness of their boards, sometimes (and particularly in the not-for-profit sector) with titles such as 'trustees' or 'governors'. For many organisations, large and small, appointing NEDs has now become standard practice. It is no longer limited to very large organisations and there is increased focus on the professionalism and training of NEDs.

NEDs should make a substantive and measurable contribution to the effectiveness of the board they belong to. A NED is not a consultant or special adviser, but should, within the remit of the role, play a full and active part in helping an organisation to succeed. Irrespective of the skills, experience and contacts that NEDs will bring, they must, above all, provide appropriate independent and constructive challenge, while supporting the management team in achieving the corporate mission and the strategic objectives.

For appointments to work effectively, both the organisations and the NEDs themselves must understand the purpose of being a NED, within the specific organisation concerned, and what value the NED is expected to bring. This goes beyond statutory requirements. Organisations should not appoint a NED as an alternative to acquiring a contractor, consultant, interim or permanent staff.

The effectiveness of NED appointments, and how these are achieved, will vary considerably between different organisations, depending on their size, sector, business maturity and the nature of the challenges which they face. For example, many smaller organisations are now appointing NEDs to bring in wider experience and expertise, in response to the increased complexity of the business and organisational challenges they face.

The role of the NED is also diversifying. With the pressure on organisations to compete globally, deal with digital transformation and respond to rapidly

changing market conditions, new skills and backgrounds are needed in the boardroom. This implies a need to refresh the NED pool, bringing in new external experience and challenge when the organisation needs it, and adjusting as circumstances change. It will be an important part of the functions of a board (or, in larger organisations, a nomination committee established by the board) to identify the particular qualities which may be required of those who may join their boards as NEDs and to establish suitable succession planning procedures to ensure the maintenance of an appropriate mix of directors on the board.

Much existing guidance on the role of a NED is considered from the viewpoint of larger organisations with an established tradition of appointing NEDs. We want this guide to be helpful not only to experienced NEDs in large organisations but also the many new NEDs in small organisations, some of whom may not even consider themselves to be NEDs – for example, a trustee to a charity, a long-term adviser to a small business or a college governor.

The internet abounds with information for NEDs in every sector on legal and regulatory matters. We have therefore focused less on statutory obligations, and more on the broad mix of behaviours, skills and experiences required of an effective NED. Written by NEDonBoard, this guide is also truly independent, with no allegiance to any specific sector or business sponsor.

Above all, we want to encourage more people to become NEDs and more organisations to appoint them. We see this as mutually beneficial to private businesses, the public sector and to charities and academia, as well as to public companies. NEDonBoard hopes this will support career development of professionals in every sector who could benefit from the valuable experience of taking on a NED role.

The Selection of NEDs: Drivers for Change and the Motivations of Those Concerned

Why Should You Consider Becoming a Non-Executive Director?

Typically, a NED will offer broad experience in fields relevant to the activities of the organisation to which they are appointed. For many prospective NEDs, this is an opportunity to apply their existing experience in a wider context. But it also calls for the development of new skills, and the use of existing skills in new ways.

This will provide a NED with the satisfaction of operating with a broader perspective, and with more strategic responsibilities. When carried out in conjunction with an executive career in another organisation, NED roles can provide balance to the operational, day-to-day responsibilities of a management role.

But being a NED is not an easy option. It carries onerous legal responsibilities and may require the NED to think about, discuss and make decisions on a wide range of issues, possibly across a number of different disciplines. It also requires flexibility and sufficient available time to carry out the role, and any remuneration is expected to cover all the responsibilities of the job. Remuneration is not determined by the hours worked as in a contractor activity.

A NED must normally be able to remain independent, taking an objective view of the organisation which recognises that it is the role of the executives to run the enterprise on a day-to-day basis. For some people embarking on a NED career, it can be frustrating to have to operate by means of challenge, advice and influence rather than instructing and leading a team as an executive. The role of a NED typically requires experience of leadership, diplomacy, patience and self-motivation, along with coaching, influencing skills and emotional intelligence.

Therefore, being a NED is not the right choice for everyone. In particular, it may not suit those with a strong urge to manage a business in a hands-on way. So, before taking a NED role, it is best to consider whether you will feel comfortable with this situation. Some people feel that if they carry responsibility for the actions of the organisation as a director, they want a closer involvement than is normally possible as a non-executive.

However, if you can manage the transition effectively, there are many rewards in becoming a NED. It attracts status, it broadens your network and gives varied and new experiences. It can also strengthen a CV, leading to other appointments and career opportunities. It may introduce you to new sectors and new ways of working, creating more variety in your working life. It may be possible to build up a portfolio of roles, which can complement each other if they are in similar fields or require similar skills, although a portfolio of varied roles can also be useful, giving the NED a broad perspective. To some, NED roles are a welcome change from having to focus on the operational aspects of an executive job. But it would be a mistake to assume a NED does not have to master complex and detailed material, often in lengthy board papers that need to be read in a short time.

NED positions may give you more independence, variety, flexibility and work-life balance. Commercial NED roles are normally paid. Whilst the income is likely to be materially less than for an equivalent level executive, there are other compensating factors.

Importantly, it should be possible for aspiring NEDs to select roles which provide the satisfaction of 'giving back' to society generally or to sectors which they have benefited from, or where they have a personal interest. An old saying is that there are three phases of life: "we learn, earn, and then return". For many, being a NED falls into the latter category. This is not to say you will not still learn a lot from doing the role.

The Company's Perspective: Why Appoint a NED?

The main reasons for appointing a NED are to bring independent perspective and objectivity to the board. The legal responsibilities of all directors are the same (discussed further in the section 'The Basic Principles NEDs Should Apply'). For unquoted or non-regulated businesses, there may not seem to be compelling reasons to have NEDs on the board. However, NEDs are often valuable because they bring perspective and experience from outside the business, as well as personal connections. They may also contribute a longer-term perspective to board discussions and provide additional focus on ethical leadership.

External experience in the sector, or with customers or regulators, is particularly valuable as it should improve the understanding and management of the risks in the sector and help support business growth. NEDs can also bring diversity of skills and interests to the board whereas the experience of the executives may be homogeneous. This is particularly true in large organisations with an executive team grown from within or recruited from similar organisations. NEDs bring new styles of working, diversity and – for a young executive team – maturity. Conversely, many organisations are seeking younger NEDs who may bring in additional experience e.g. in the digital field.

In providing balance to the executives and an independent perspective, NEDs will be expected to provide challenge to executives on the board, keeping the interests of shareholders and other stakeholders particularly in mind. The independent perspective which the NED will bring is one of the principal reasons why NEDs are likely to chair (and comprise the membership of) the risk, audit and remuneration committees of the board, as these committees have specific roles in holding executive management to account. The involvement of effective NEDs is an important reassurance to regulators and investors, and may encourage shareholders or bondholders to increase their investment. In start-ups, the NEDs will often bring an investment stake and introduce others.

Another potential advantage of having NEDs is the possibility of their capacity to sponsor projects. While it may not be helpful for a NED to act formally as a consultant, NEDs may nevertheless be able to provide a similar service, at least at the start of a project, and the company then has the benefit of a trusted resource with an open-ended commitment to the company and normally at no extra cost. This is often particularly relevant to start-up businesses, but also applies in larger organisations.

NED Roles: A More Detailed Review

The Commonalities and the Differences

NED roles vary greatly, due to factors such as:

- **The sector.** There are many different sectors - not just the public and private sectors, and different business sectors, but also charities, academic institutions and professional bodies, all of which have different cultures, regulations and functions.
- **The type of business.** A family-run business or a partnership, compared with a large corporate for example, will probably require a very different style of NED.
- **Other factors.** Such as the balance of the number of NEDs and executives on the board. Some boards have a NED majority; some may have just one NED brought in for a specific role.

There are a variety of secondary characteristics which also impact on NED roles, such as:

- **The nature of business challenge and the phase of the business life cycle in which the company operates.** An organisation may be going through a merger or an acquisition, or may be operating in difficult times, perhaps with strong competition, market change and pressure from shareholders or financial backers.
- **The scale of the business.** A small business or 'start-up' will need a different skill set, which may be more intense or specific than is expected of a NED in a large, well-established and mature organisation.
- **The balance between UK based and international activities** can make a difference as well, especially in organisations operating internationally or entering a new market overseas.

- **The regulation of the business activities** may impact the NED role. For example, in the financial sector, NEDs caught by the Senior Managers & Certification Regime must have their appointment pre-approved by the Prudential Regulation Authority and the Financial Conduct Authority.

The importance of culture within an organisation is increasingly recognised. Organisations differ from one another in the processes, style, culture, and behaviours of the leadership team, irrespective of the sector. NEDs will need to be aware of this: they may have the opportunity to help develop a better culture within the organisation they join, and they may perhaps need to adapt their personal style to fit within an existing culture.

In other words, a NED does not just bring business skills and experience; their inter-personal and 'soft' skills matter too. Some environments require consummate political sensitivity, some an open, fast-moving, 'no holds barred' and 'pull no punches' approach.

Some NED roles are paid, and some are pro bono. This should not make a difference as to how NEDs carry out their duties, but a volunteer role may be perceived differently in practice.

Some NED roles are not necessarily regarded as such e.g. charity trustees and college governors are not always regarded as non-executive directors, although their functions and general legal responsibilities are frequently very similar to those of the NED in a commercial organisation.

Understanding these issues, and the distinctions between different roles, help a NED perform well - to challenge constructively, to understand the demarcation of roles of executives and NEDs, and to avoid some of the cultural, business and legal pitfalls which arise.

Types of Organisation

Companies are all required to have directors, as are "mutual" bodies. Other types of entity may not have directors as such but are led by those who operate in a similar capacity, including some partnerships.

Many charities are set up as companies, most commonly as "companies limited by guarantee" (while most commercial companies are "limited by shares"). The "members" of companies limited by guarantee have some of the same functions as the shareholders in a commercial company including the right to appoint and remove directors but have no financial stake in the company: they may however be required to contribute (to "guarantee") some purely nominal sum to the company if it becomes insolvent.

Trustees of charities which are constituted as companies limited by guarantee or as "charitable incorporated organisations" (an alternative form of charitable organisation) will be regarded in law as directors of their organisation, although they are normally referred to as charity trustees. Charity trustees have specific legal obligations which do not apply to directors of commercial companies, and trustees of corporate charities will need to be familiar with these (as well as their duties under company law).

Community Interest Companies, organisations set up under special rules to carry out a social purpose, but not strictly charities, are also normally companies limited by guarantee.

There are various types of "mutual" bodies whose constitutions may be similar to companies, but with some different features.

Professional organisations and increasingly firms in the financial sector are often constituted as limited liability partnerships, which share many of the features of a limited company with boards on which NEDs may participate.

Entities can also exist with less formal status, such as unincorporated associations – many local sports clubs and community organisations are constituted in this way, for example. People taking leadership roles in these types of organisations need to consider what legal liabilities they may be assuming, as they differ from those of directors of formally incorporated bodies such as limited companies.

Sectors

The Private Sector

Many people looking for a NED role will think first of the private sector, because that is a world with which many in this position feel some familiarity and also because NED roles in the private sector are more likely to be remunerated (or perhaps better remunerated) than elsewhere. The qualities and benefits which NEDs are recognised as adding in private sector roles, including individual skills and experience, contacts and profile, are now sought after in other sectors as well.

The requirements for a NED in any company will of course vary, depending in part on the scale and nature of the company's operations. Small and medium sized enterprises (SMEs) and start-ups often appoint NEDs to bring in specialist skills and to overcome specific challenges, as well as contributing by bringing contacts and influence. Sometimes, an organisation, such as an SME, may be too small or too immature to employ full time executive directors with the complete set of skills required, or they may be simply changing too fast, such as a start-up business. As in other sectors, a NED can widen and complement the board's effectiveness, reducing pressure on executives to know and do everything.

The Public Sector

The public sector is very varied, with NED roles found today in every area – councils, government departments, non-departmental public bodies (NDPBs), schools, colleges, universities, police and fire services.

Health organisations, local authorities and many NDPBs appoint NEDs, some extensively. In some cases, public service organisations are already working with a private sector partner, such as an advisory or consultancy business which provides NED-type input.

Many local authorities, government departments and NDPBs set up trading bodies, often to draw in new income as public sector budgets and grants are cut.

They use this mechanism to sell new services, increase revenue generation and collection, and to underpin integrated shared service arrangements. They look to NEDs to provide commercial and business practice experience, as well as an understanding of public service ethos and regulation. Their operations may extend beyond trading, and the skills they may seek from NEDs may include mergers, acquisitions, sales of businesses, structuring of complex contracts and setting up public and private partnerships.

Academic Sector

Universities, colleges, schools of all types (public, private and state sectors) and associated research bodies, often appoint NEDs. Sometimes they are called governors, sometimes trustees, but they are all in effect NEDs.

There is extensive guidance on the internet for state sector college and school governors, and NEDs in this sector are advised to be clear on the specific role they are taking on, in addition to making themselves familiar with the general guidance. This is because whilst the guidance is good, the nature of specific roles varies, and organisations have different understandings as to what they may expect from their NEDs. This will affect the NEDs' risks, responsibilities and liabilities.

Third Sector

The Charity or "Third sector" is diverse and complex. According to Charity Commission data, there were nearly 170,000 (as at September 2018) registered charities in the UK. Some are linked together, sharing trustees. Many are small, not-for-profit community organisations falling outside the legal requirements for registration, but many are large and at least as complex as listed public companies. Some include the running of businesses within the scope of their overall charitable activities, with sales, marketing, product development and customer services.

There are some excellent guidance notes for aspiring NEDs in the charity sector published by the Charity Commission (see Appendix).

Special Roles a NED May Hold

Chair

The Chair leads the board and is responsible for it working effectively. He/she sets the agenda and ensures that it is properly dealt with in the meetings.

The Chair will also be responsible for ensuring that there is a constructive and appropriately collegiate relationship between board members. This will involve ensuring that all board members have the opportunity to participate, and that a good dialogue takes place between NEDs and executive directors. The Chair should ensure that healthy debate and constructive challenge take place, without becoming unnecessarily or unhelpfully divisive.

The Chair is also responsible for communications with shareholders and for the relationship with other stakeholders.

The role of Chair is distinct from the role of the Chief Executive Officer (CEO), who runs the business. The Financial Reporting Council's (FRC) UK Corporate Governance Code expects the roles to be held by different people and discourages transition from CEO to Board Chair.

In other countries, notably the US, the roles of CEO and Chair are often combined. This may also happen in the UK in special circumstances, for example where strong leadership is required in difficult times for the company, and particularly in smaller companies with simpler operating structures.

Typically, the Chair will be experienced in leading a mixed team of senior professionals, carrying status and gravitas, with political skills, emotional intelligence and sound understanding of corporate governance.

NEDonBoard has published a Board Best Practice® guide focused on the role of the Chair. The publication is available upon request to members of the NEDonBoard community.

Senior Independent Director

In 2003, the Higgs Report recommended that one director should be designated as the Senior Independent Director (SID), and this role is now formally recognised in the UK Corporate Governance Code. The SID is effectively a champion for the NEDs and, where required, a channel for communications with shareholders, independently from the Chair. The SID may also on occasion act as an alternate to the Chair.

The SID will also organise the appraisal of the Chair's performance, whereas appraisal of other directors (as required under the UK Corporate Governance Code) is carried out by the Chair.

UK Government Corporate Governance Reforms

A major part of the UK Government's Corporate Governance reforms, introduced in 2017 by way of response to a November 2016 Green Paper and now mostly implemented, was to urge companies to engage more directly with their work forces. One suggested possibility for companies to do this was through the appointment of a NED designated with responsibility for engaging with the workforce. Such an arrangement, along with other possible alternative methods to encourage workforce engagement, is now suggested in the UK Corporate Governance Code, although it is not known at this stage how widely the particular idea of a NED with these specific responsibilities will be accepted.

Advisory Councils

It can be useful, as a way of preparing for NED roles, to act as an observer on a board or to join an advisory council. This provides practical experience of how boards function. It can help people decide if they would enjoy board responsibility and facilitate their transition from executive to non-executive roles, without them needing to accept formal appointment and responsibility for the board's decisions. A number of boards, particularly in the charity sector, offer such volunteering opportunities. In some cases, young companies may value an advisory council as a way of mentoring the board.

However, care should be taken, particularly by members of advisory boards (and by consultants at board level) that they do not become so extensively and intimately involved that they make themselves accountable in the same way as formally appointed directors by becoming "shadow" or "de facto" directors. A shadow director is defined in the Companies Act as someone in accordance with whose directions or instructions the company's directors are accustomed to act, but would not, for example, include someone acting in the capacity of a professional adviser. Complex legal issues may arise in this area.



The NED Journey: From Appointment to Success in the Role

Factors You Should Consider Before Accepting a Role

Applying for a NED role, being asked to attend a NED interview, or indeed being offered a position, is exciting and flattering. There is often stiff competition and you will be selected because of your reputation or experience. But you should be careful before accepting a position and consider the following points in particular:

- **Your level of interest and commitment to the organisation and to the role.** Most appointments require review and re-election after three years but there may be an expectation that the NED will complete at least two three-year terms, or even three. While it is possible to step down earlier, this might damage your future prospects generally, and will limit the value you contribute, compared with completing a normal term of office.
- **Personal risk.** It is crucial to assess the risks and whether you have the requisite sector and governance skills to shoulder responsibility for them. Ask if the business will provide training ask for the details of the NED on-boarding process and ask whether D&O insurance has been obtained on your behalf. Consider whether the experience of the other NEDs will complement any limitations in your own experience. Many not-for-profit enterprises such as schools and hospital trusts say that sector experience is not necessary for their non-executive roles, but you may still be criticised by the public or regulatory bodies if they regard you as unsuitable for the role.
- **What resources does the organisation offer?** Do they offer formal induction and training both before starting, and ongoing? Can they support you with appropriate professional advice, including legal advice if there are legal or regulatory challenges? While a major PLC will take this for granted, it may be more difficult for a start-up to resource this. Prospective NEDs should however ask for some form of induction in any case, since it will enable them to make a more effective contribution from the outset. The possibility of continuing training, as expected by the UK Corporate Governance Code, should also be investigated. We note that NEDonBoard through its Board Best Practice® publications and events offer ongoing professional development opportunities to NEDs and Chairs.
- **Time commitment, travelling requirement, fees, and expenses all need to be fully understood.** It is a good idea to ask existing NEDs about the time commitment if you can, as well as asking the company itself: NED roles can be extremely demanding as regards the necessary time commitment required.
- **Letters of appointment.** There are sample NED letters of appointment online, or you may prefer to take your own legal advice. NEDonBoard provides its standard letter of appointment as well. In addition to checking that a letter of appointment correctly sets out the NED's expected time commitment and remuneration. NEDs should seek to ensure that their contract makes appropriate provision for their indemnification and insurance (as discussed further below), and for their protection in the event of any dispute.
- **The implications of the legal and regulatory status of the organisation.** For example, directors of banks and insurance companies have additional responsibilities to the regulators, and some potentially onerous personal liabilities under the Senior Managers and Certification Regime. The liabilities of partners in established partnerships are subject to particular legal considerations.

In order to assess the liabilities you are taking on, it is important to understand thoroughly the insurance cover that the organisation provides to NEDs and to executives ("Directors and Officers cover" – D&O), as you may need to fall back on that. It is advisable to find some benchmarks to compare with and consider if your insurance cover is sufficiently comprehensive.

You should also ask if D&O claims have been made in recent years, and how much of the overall liability cover is still available. Bear in mind that the D&O cover cannot cover all liabilities, and it may be advisable to take out additional insurance. Various contracts are available and are increasingly being used by regulated businesses to protect both their executives and NEDs.

Conducting thorough due diligence prior to accepting a NED role is of great importance as your reputation is at risk; and what you learn from due diligence may greatly assist your effectiveness as a NED as soon as you are appointed.

In summary, carry out your own personal due diligence about the role, especially in the following areas:

- **Business & sector.** Strategic future, competitors, regulation, profitability.
- **The Chair and other NEDs.** Their integrity, resilience, openness, likeability.
- **The executive directors.** Integrity, understanding of the business, future commitment.
- **Legal and regulatory status.**
- **Terms and conditions and protection** available to you - Including D&O cover.

The Basic Principles NEDs Should Apply

There are various key governance principles that all directors must be aware of: the principles of the Companies Act Sections 170 to 181.

These sections, which form part of a wider set of rules governing directors in Part 10, Chapter 2 of the Companies Act, cover executives and NEDs on an equal basis. There are seven "general duties" set out in the Act, and directors should be familiar with these.

The most important duty is "to act in the way [the director] considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—

- a) the likely consequences of any decision in the long term,
- b) the interests of the company's employees,
- c) the need to foster the company's business relationships with suppliers, customers and others,
- d) the impact of the company's operations on the community and the environment,
- e) the desirability of the company maintaining a reputation for high standards of business conduct, and
- f) the need to act fairly as between members of the company.

This, the "Section 172 duty", has received particular attention in the UK Corporate Governance reforms referred to above, and before that in the FRC's paper on "Corporate Culture and the Role of Boards", partly because the matters to which directors of a company are to "have regard" cannot be legally enforced by employees and other stakeholders directly affected.

The Government reforms in this area have been implemented by the imposition of additional requirements on large companies to report on the ways they have fulfilled their Section 172 duty, and by the publication of guidance by ICSA and the Investment Association on stakeholder engagement to which directors of all companies should pay attention.

The general duties owed by a director of a company to the company – Companies Act, 2006

- 171) Duty to act within powers
- 172) Duty to promote the success of the company (with subsection (1) stated in main text above)
- 173) Duty to exercise independent judgment
- 174) Duty to exercise reasonable care, skill and diligence

- 175) Duty to avoid conflicts of interest
- 176) Duty not to accept benefits from third parties
- 177) Duty to declare interest in proposed transaction or arrangement

For full statements of duties, please refer to these directly in the Companies Act.

The Companies Act also requires directors to obtain shareholder approval for some dealings with the company, including entry into a service contract, some property transactions, and loans. They are also responsible for meeting a range of reporting obligations.

NEDs need to bear in mind that directors can be held personally liable for breach of their duties in a range of situations; these include acting beyond their powers, failure to use sufficient skill and care, ignoring conflicts of interest, trading when the business is or is likely to become insolvent, fraudulent activities and serious health and safety shortcomings. The potential penalties can include criminal sanctions or disqualification of directors in some circumstances.

All directors may also incur personal liability outside the Companies Act, for example, for breaches of environmental, health and safety, and competition law, depending to some extent on the nature of their company's business.

Other Codes and Guidance

In addition to the Companies Act, there are a number of specific codes and sources of guidance, several drawn up for use by specific types of company.

- The **UK Corporate Governance Code**, published by the Financial Reporting Council (FRC), which applies specifically to premium listed companies but many of whose principles are reflected in other governance codes, and which contains principles which many non-listed companies aim to follow where they are relevant.

The UK Corporate Governance Code has been substantially amended, and the new version published in 2018 has taken effect from 1 January 2019. It has taken effect in conjunction with the FRC's new Guidance on Board Effectiveness, amended and republished at the same time.

- The **Quoted Companies Alliance (QCA) Corporate Governance Code** published by the QCA and intended for smaller listed and AIM quoted companies. Since the AIM rules were amended in 2018 to require AIM companies to follow a recognised governance code, it has become the code most widely used by AIM companies.
- The **Wates Corporate Governance Principles for Large Private Companies** published by the FRC in 2018 at the instigation of the UK Government as part of its package of governance reforms.

- The **Charity Governance Code**, published by leading institutions in the charity world, in separate forms for large and small charities, and backed by extensive material for charities and their trustees published by the Charity Commission itself.
- The Education Funding Agency (EFA) provides guidance for governors of schools which are maintained within the state education system.
- NHS Improvement is responsible for overseeing NHS trusts and foundation trusts; their website provides an array of relevant guidance.

Many other types of organisation will have specific guidance and the NEDs should ensure they are familiar with this guidance.

Directors of London Stock Exchange listed companies will need to be aware of the rules and regulations set out in the FCA Handbook, and directors of AIM companies need to be aware of the AIM Rules for Companies. Directors of both listed and AIM companies will also need to be aware of the EU Market Abuse Regulation, particularly in connection with rules relating to the release of information into the market and dealings in their companies' shares. (The precise status of the Market Abuse Regulation, following the UK's withdrawal from the EU is not known at the time of writing.)

General Guidance for NEDs

The following final sections are intended to help a NED to make best use of their individual strengths and competencies as well as their personal style in exercising the role:

- Take a strategic view. This is important for all directors, but many executive directors will also have a focus on their specific areas of executive responsibility, whereas a NED should take a broad view on all subjects; they should not confine themselves to areas of personal expertise.
- NEDs should use their wide external experience for the benefit of the organisation.
- NEDs should bring an objective perspective to the governance of the organisation. This involves remaining independent from (but supportive of) the executive management of the company, and having the courage to stand up to them when necessary.
- The NEDs' independence is particularly important in exercising their Companies Act responsibilities towards external stakeholders – shareholders, employees, customers and the environment.
- NEDs should respect the distinction between the governance responsibilities of a director and the executives' responsibilities to run the business, while appreciating this is not clearly defined and requires the exercise of discretion, according to circumstances, as indicated in the Walker Report.
- NEDs should hold the management of their company to account.

"In broad terms, the role of the NED, under the leadership of the chairman, is: to ensure that there is an effective executive team in place; to participate actively in the decision-taking process of the board; and to exercise appropriate oversight over execution of the agreed strategy by the executive team."

Walker Report, 2009

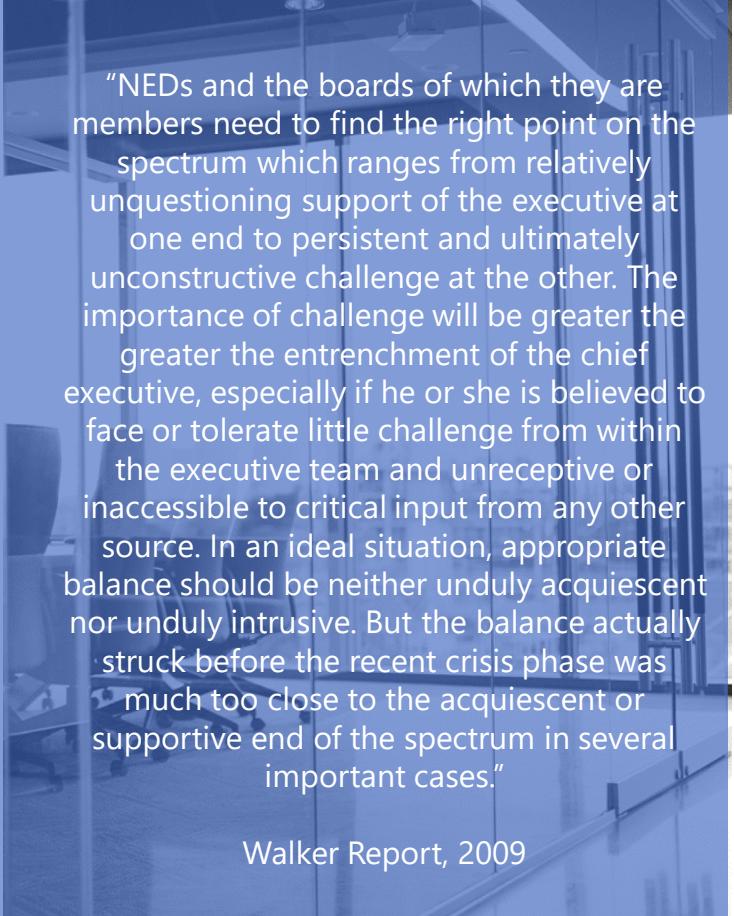
"An over emphasis upon monitoring and control risks non-executive directors seeing themselves, and being seen as, an alien policing influence detached from the rest of the board. An over emphasis on strategy risks non-executive directors becoming too close to executive management, undermining shareholder confidence in the effectiveness of board governance."

Higgs Review, 2003

NEDs should also:

- Apply intellectual curiosity, such as reading around the subjects relevant to the activities of the board, meeting a range of people both within the organisation, and external stakeholders.
- Be sufficiently determined and conscientious to ensure they are receiving a full and honest report on the business of the company and that questions are being properly answered.
- Be constructive in the way they challenge – clear, positive, and bringing new ideas.
- Be aware of the right time to step aside – either at the end of an agreed term, or before that if there are issues of principle the NED cannot support.

The next section provides guidance on *how* these responsibilities might be carried out.



"NEDs and the boards of which they are members need to find the right point on the spectrum which ranges from relatively unquestioning support of the executive at one end to persistent and ultimately unconstructive challenge at the other. The importance of challenge will be greater the greater the entrenchment of the chief executive, especially if he or she is believed to face or tolerate little challenge from within the executive team and unreceptive or inaccessible to critical input from any other source. In an ideal situation, appropriate balance should be neither unduly acquiescent nor unduly intrusive. But the balance actually struck before the recent crisis phase was much too close to the acquiescent or supportive end of the spectrum in several important cases."

Walker Report, 2009



How to Conduct Yourself as a NED

Once you are appointed as a NED, you are likely to find that you need to adjust in various ways, particularly if you are making a transition from executive life.

Most NED candidate specifications will insist that the candidate should have utmost integrity and probity, but this does not necessarily preclude people from companies that suffered public criticism, from getting NED roles elsewhere. NEDs will need to be ready to respond to any questions regarding their past career and how it relates to their NED role.

Remember also that if you are a NED in any organisation with a public profile, your comments and views, however light-hearted or well-intentioned, may be reported in social media or quoted privately to your or the company's disadvantage. So, take care! Demonstrate integrity in both your corporate decision making and general way of life. This is not a good time to get involved in an undignified Twitter spat or even an emotional row with the neighbours, as that could be used against you and the organisations you work with.

Utmost confidentiality about the enterprise's internal discussions is essential at all times. Any dialogue with stakeholders and the outside world about the company and its business requires careful handling, must be planned and thought through, particularly for listed companies. NEDs need to apply judgment.

Loyalty and responsibility to the business comes first, and it is essential that conflicts of interest be avoided, or when they arise disclosed so that legal requirements and the company's own constitutional rules (as set out in its articles of association) are complied with.

Even if a NED is appointed by a particular shareholder or by a stakeholder group (and in some countries, this may include trade unions) his or her responsibility, in the UK at least, is to all the stakeholders. Note that no responsibilities are owed in law to stakeholders though under s.172. of the Company Act, directors are encouraged to consider all stakeholders. This means the NED should use his/her judgment to make contact with, and listen to the views of, shareholders, customers, employees, sponsors, partners, local community, regulators and creditors so that he/she is informed with the business as deemed necessary to fulfil the NED duties.

A NED should also take advice where it is needed and should not rely solely on his or her own judgment. It is not sufficient to rely on opinions from the "golf club" or social media. Whilst broad personal experience is part of the benefit of employing a NED, it should not lead to blinkered subjectivity, personal crusades or a narrowing of perspective. Normally professional advice would be taken by the business itself, not the NED, but a NED should not hesitate to request it where appropriate.

Although the business may provide ongoing training, a NED should take personal ownership for their professional development. With the effectiveness of boards at the core of the NEDonBoard mission, we consider that the ongoing professional development of NEDs and Chairs is essential. NEDonBoard runs Board Best Practice® initiatives on a range of boardroom topics and invite keynote speakers and boardroom experts to share their expertise at its events. You need to be fully aware of your statutory obligations, and the skills required to fulfil the role you have taken on, since if things do go wrong, ignorance is not an acceptable defence.

And there are many ways to keep up-to-date. NEDonBoard provides connection, knowledge and authority to the community of non-executive directors and board members and numerous opportunities to learn through the events or Board Best Practice® publications. Specific industry organisations and bodies also address NED related topics. There is also ample material online, both the standing material on NED's responsibilities in general, and publications and webinars on current topics, such as Government budgetary announcements, constitutional developments including Brexit, and targeted industry matters.

Allow sufficient time to prepare for and to follow-up from meetings, and also to keep abreast of the business itself and the sector. The role requires more than attending the formal meetings, and a greater engagement will make constructive challenge more effective as well as the role more fulfilling. Often the NEDs themselves will meet separately from the rest of board, to assess the effectiveness of the board and reflect on the executives' performance and succession plans.

The NED's role is to challenge, but always to do so constructively. This means coming up with ways to

solve problems, not just to expose them. This may require meetings with executives outside the main board, so you can understand their perspective on a particular topic and build personal relationships (without of course, compromising objectivity).

Your behaviour on the board must remain objective but decisive, applying honest and independent judgment. Do not just follow the lead of the executives or other NEDs even if they are more experienced or longer-serving than you. CEOs by their nature tend to be strong personalities, and NEDs need to be able to stand up to them. But equally, the board is not the place for rows of a personal nature or intransigent behaviour.

A NED also has a role to mentor and even inspire management, and to give them appropriate encouragement and support. It is important to remember this not just in relation to executives on the board but also as regards management below board level: when presentations are made to the board, which may have involved a great deal of preparation, NEDs should react courteously and with interest.

It is also strongly recommended for a NED to not form particular alliances within the executive; a NED must be, and be seen to be, at all times, totally transparent, objective and independent.

A board has collective responsibility for its decisions. If after constructive debate and a genuine attempt by all sides to understand each other's points of view, it is impossible to reach consensus, then a board member (including a NED) may well feel it is important for the minutes to record that they do not support a decision. If the issue is sufficiently critical to the running of the business, for example, where there is continuous disagreement on strategy or policy, then the board member may feel the need to resign.

It is rarely professionally appropriate to share this discussion and disagreements outside the boardroom, however strongly felt. However, where the departure involves potential breaches of ethics or law, it may be appropriate to inform appropriate regulators, and in extreme circumstances it may be advisable for the NED to take advice on their own personal position. In a regulated business, the regulators will expect a frank explanation from any director who leaves the board unexpectedly. Major investors will also normally seek a confidential discussion with directors in such circumstances.

Above all, NEDs should not try to do the executives' job although they do need to understand what the executives are doing, maintain oversight over their activities and hold them to account. Occasional deep dives are valuable to improve a NED's understanding, and there will be occasions where a NED has to become more closely involved in order to fulfil their responsibilities. It is normally helpful to frame input as questions or suggestions, as opposed to instructions, although you need to ensure your points are heard and acted upon. A difficult balancing act - but also an interesting challenge!

Follow these hints and your reputation, contribution and views will be accurately conveyed around the organisation, and not seen to be biased towards a specific agenda, team or personal interest. As you would in executive roles, be discreet, and treat other directors on an equal basis. But above all be yourself and enjoy the role!



Appendix

References

Non-executives are responsible for familiarising themselves with the regulatory and legal responsibilities of their role and sector.

The below list is not exhaustive however, it highlights some useful reference points.

- **Companies Act, 2006:** [link](#)
- **The UK Corporate Governance Code:** [link](#)
- The **QCA Corporate Governance Code**, available for purchase through the QCA website
- The **Wates Corporate Governance Principles** for Large Private Companies: [link](#)
- The **Charity Governance Code:** [link](#)
- The **Charity Commission, The Essential Trustee:** What you Need to Know, What you Need to Do: [link](#)

Useful Further Reading

A Guide to Directors' Responsibilities Under the Companies Act 2006, ACCA: [link](#)

City Values Forum and Tomorrow's Company, Governing Culture: Risk and Opportunity, September 2016: [link](#)

Guidance on Directors' Duties- Section 172 and Stakeholder Considerations, published by GC100: [link](#)

The Stakeholder Voice in Board Decision Making, published by ICSA: the Governance Institute and the Investment Association: [link](#)

Government response to green paper on corporate governance reform: [link](#)

Insolvency and Corporate Governance reform – UK Corporate Governance response: [link](#)

For details relating to the certification of senior managers in the financial sector regulated by the PRA and the FCA: [link](#)

The UK Stewardship Code, 2012: [link](#). We note that the FRC published a consultation on the draft 2019 UK Stewardship Code on 30 January 2019. An updated UK Stewardship Code will be published in the summer 2019.

Guidance on The Strategic Report, 2018: [link](#). This is one of a number of formal Guidance notes published by the FRC: others include Guidance on the Audit Committee, Risk Management and Reporting and Board Effectiveness, and you can find all of them on the FRC website.

Liability of Non-Executive Directors: Care, Skill and Diligence, ICSA: [link](#)



NEDonBoard Resources

NEDonBoard blog: [link](#)

NEDonBoard library: [link](#)

Board Best Practice® publications: [link](#)

UK Corporate Governance Code, an evening with the Chair of the FRC: [link](#)

Understanding your NED legal duties, liabilities and due diligence, NEDonBoard expert panel event: [link](#)

Reviews and Reports

The Cadbury Report, The Financial Aspects of Corporate Governance, 1992: [link](#)

The Higgs Review, Review of the Role and Effectiveness of Non-Executive Directors, January 2003, Derek Higgs: [link](#)

The Walker Report, an independent review of corporate governance in the UK banking industry, November 2009, Sir David Walker: [link](#)

For some of the latest thinking around diversity issues at board level, see:

The Hampton-Alexander Review on FTSE Women Leaders: [website](#)

The Parker Report into the Ethnic Diversity of UK Boards: [website](#)

Thank you

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If you have any questions related to this document, our contact details at NEDonBoard are team@nedonboard.com.

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