

## How to choose your first NED role



*I gave a nervous laugh. The headhunter had just suggested that I could start my non-executive career by joining Northern Rock.*

*Why would I want to join the board of a bank suffering a run, the first British bank for over a hundred years to experience one?*

NED appointments are not for life, but they are generally expected to last two terms of three years, and any less will leave you permanently having to explain why not. You can't easily take one up, and resign a year later, so it's not like an executive appointment. It should be treated as a six year commitment.

This means that you need to do your due diligence very carefully, looking hard at the company, its shareholders and the existing board.

### **The Company**

Companies come in all shapes and sizes and so do their competitive positions. Some NED's are sizeist. They only want to be involved in companies of a big enough size. However, my experience is that smaller companies are often more interesting and the boards get involved more in business issues. The largest companies seem to have bigger boards and more time spent on governance compliance.

A future non-exec should be sure that they are happy with the company's prospects, product and philosophy;

1. **Is the market, in which the company operates, growing?** It is difficult to consistently grow market share in a stagnant or declining market, so if you want to be involved in a growing business, this is pretty important.
2. **Does the company have a sustainable competitive position in its market?** This is not only about growth, but also about sustaining a company's current position. Most people want to join a company that can grow and outperform. If you join a company in decline, the NED role is likely to be much harder and there will be many tough decisions to make.
3. **Are you interested in the product?** Although you would not be involved in day-to-day in operations, board meetings can be terribly dull if you have no affinity with the product. I found it difficult to get excited about banking, but find aviation fascinating. If you are a consumer person, then a heavy manufacturing board would probably be very tedious to you. If you are very interested in digital and IT, then perhaps a mining business

wouldn't be right for you. This is a good place to be honest with yourself, about what really interests you.

4. **Is the business at risk of cash problems?** Companies don't go bust when they make a loss, it's when they run out of cash. They can get liquidity problems even while making a paper profit. Have they got enough cash or debt facilities? This should be an easy question for a financially-trained candidate, but everyone must ask it. The simplest markers are; is profit projected to rise or fall? What is the level of gearing (debt/net assets: and debt to debt plus market capitalisation)? Is the business using cash (ie is net debt rising)? What do analyst reports say (a good headhunter will send you some)? If a company is in financial difficulty, the NED role will be much busier, and you will bear some risk. Personal financial liability is potentially uncapped for all directors when their company trades on whilst insolvent. I forgot that when I joined Northern Rock!
5. **Do you like the philosophy/culture of the business?** You might not approve of gambling, tobacco or arms manufacturing, so this would be an immediate red flag for you. It may be that you get the impression that the business puts profit before people, or has a poor compliance record in some areas. This may be more subjective, but it's worth asking around in both the market in which it operates, and also bankers and other headhunters. You'll normally get a good feel from their immediate response, particularly if it's a short silence while they work out how to say something tactfully. Googling the company will uncover critics of the company.

### **The Shareholders**

I'm often asked if I prefer being on the boards of public, private or private equity companies. The big difference is not the ownership structure however, but the shareholder make-up. Broadly speaking, if you have a shareholder, or grouping of shareholders, with more than 30% of the stock, be aware that they could exercise great influence on the board. If they are activist in some form (all private equity can be classed as activist), then the chances are that they will exercise that power at some point. Shareholders own the company; the board merely manages it for them.

### **The Board**

If you are happy with the company, then think about the existing board. This may be in a steady state and your appointment could be a direct replacement for a time-served NED. Alternatively the Chairman, perhaps newly-appointed, could be renewing the board with wholesale changes. Both situations have their advantages and disadvantages, although expect more challenge in the latter one. If your predecessor is not obviously time-served (ie six years plus), it is well worth asking why they are leaving. If in any doubt, ask to speak to them yourself.

The most important person for the board's success is the Chairman. It is therefore a good idea to scrutinise them carefully. Do they understand the

business? Would you like working with them? Would you learn from them? Will they be strong enough to keep the board and CEO in check?

The role of the Senior Independent Director is usually important only when the board is itself having difficulties. You should satisfy yourself that they are truly independent of the Chairman, and not their buddy. The SID needs to be strong enough to take an independent, and lonely stand, if necessary. On the other hand, a SID clearly ambitious to be the Chairman is a potential issue. I was keen to join one board, until the SID explained at great length the failings of the Chairman. As the saying goes, I made my excuses and left.

The most important person on the board for the business's success is the CEO. You need to ask the other directors and form your own assessment as to how good they are. Joining a board with a successful CEO is very different to joining one with a CEO under pressure. Key to this will also be your assessment of how the Chairman and CEO get on together. The Chairman needs to keep a certain distance from the CEO, but if the two are fighting, then one of them will eventually have to go.

If two directors interview you at once, watch the interaction and body language between them, especially when you ask difficult questions. If they look at each other before answering, or one develops a sudden interest in the carpet, beware. Better that you discover any difficult board issues now rather than after you've signed on.

Look at the background and experience of your prospective fellow directors. This will tell you a lot about how the board works and what meetings will be like. An entirely male, single culture, directorate all in their 60's would send you a signal. Maybe you too are like that, and would feel comfortable, or maybe you are not and would be the 'diversity' director. Look at their CV's. Are these people that you will learn from and enjoy working with? Remember that you might be locked in a boardroom with these people for six years, without time off for good behaviour.

You might say that in joining Northern Rock, I ignored some of my own rules. Even I had spotted that the business was in financial problems, as constant TV news reports showed queues outside branches. I also discovered, by being on the board, that I had limited appetite for banking. However, it was only because they had a financial crisis, and so most experienced NED's wouldn't go near the company, that they offered me my first NED role.

I learnt a huge amount in my time on that board. So if you are offered a "difficult" board role, you may gain enormously from the experience. But don't believe everything you are told by the existing board and the headhunters, gather as much information as possible from different sources, and go into it with your eyes wide open.

Not many NED's do the job because they need the money alone to survive. Most do it, or choose a particular role because they think they will enjoy it and learn something. Do not go for one job because it pays a little higher fee or the company is bigger or more prestigious. You may well come to regret that over an extended period, whereas a fun job will always be a fun job.

## Summary

1. Regard an NED-ship as a six year appointment. Like the French Foreign Legion, you are welcomed it, but it isn't that easy to get out.
2. Research the company, read analyst notes and ask around.
3. Ask yourself;
  - a. Is its market growing?
  - b. Is there a sustainable competitive position?
  - c. Does the company interest you?
  - d. Is it in any possible financial difficulty?
  - e. Do any shareholders exercise control over more than 30% of the stock?
4. If the answer to a, b, d and e is 'no', then proceed only if you enjoy a challenge. Go in with your eyes open. If the answer to c is 'no', just say 'no'.
5. Think about the board;
  - a. Is it in stable?
  - b. Do you respect the Chairman?
  - c. Do you rate the CEO?
  - d. Do you think that the SID and other board members work well together?
  - e. Would you enjoy working with the board members?
6. If the answer to a, c and d is no, expect a challenging role. If the answer to b and e is no, say 'no'.
7. It's your NED career, in the end do what you feel is right and what you are sure you can spend six years doing.