IDEAS FOR HIGGS REVIEW

In the interests of keeping readers fully up-to-date with corporate governance issues as they develop, we summarise below some of the recommendations being made by various institutes to the Higgs review on the role of non-executive directors.

NAPF

The National Association of Pension Funds says in its submission to Higgs that non-execs should have "the courage and integrity to whistle-blow or even resign over matters of principle". Non-execs also need to have independence of mind: it is critical that non-execs be prepared "to ask necessary questions and to hold the executive to account".

The body which represents many institutional shareholders says it is also vital that non-execs be able to devote enough time to "gaining a thorough understanding of a business at all levels". It recommends that any listed company with non-execs holding more than five such positions should explain in the annual report how they are able to devote sufficient time to the job.

Board vacancies should be advertised so as to widen the pool from which non-execs are recruited.

UKSIP

The UK Society of Investment Professionals focuses on the chairman of the board in its submission to Higgs. It says that, while investors have been calling for the separation of the roles of chairman and chief executive, the chairman's role "is unlikely to have been in the performance spotlight". But effective chairmen are "crucial" to ensure non-execs have the information they need to help develop, challenge and criticise strategic planning. The chairman can also see to it that investor input via non-execs is properly discussed by the board.

The UKSIP wonders whether institutions that call for the appointment of a senior independent director are really questioning the adequacy of the chairman. It also sees a connection between the number of non-exec directorships held by any one person and the effectiveness of the board, and calls for non-execs to demonstrate "independence of mind" and to "whistle-blow". It claims that non-execs are underpaid, but that pay should not be their main driver for seeking appointment.

Finally, the UKSIP says that international companies should embrace global governance principles and should appoint non-UK non-execs.

ACT

The Association of Corporate Treasurers says that, "within the unitary board... the independent non-executive is vital and there should be a more rigid definition of 'independent director'". The chairman and the majority of the board should all be independent non-execs: in fact, the Combined Code rule that allows the positions of chairman and chief executive to be combined should be abolished.

The ACT says it is essential that non-execs should have "a greater understanding of the assessment and management of financial risk – an area where most directors have the least experience but are expected to contribute the most".

It adds that the number of directorships taken on by any one individual should be limited and that companies need to support and develop the abilities of their non-execs. The issuing of options, shares and big bonuses to non-execs should be avoided. Their personal liabilities also need to be "limited to realistic levels".

CIMA

The Chartered Institute of Management Accountants calls for a code of best practice for non-execs which should be incorporated into the Combined Code. Without it, non-execs "have no clear guidance on what their role is and how it should be fulfilled. Many non-execs rely on their own experience on other boards, and the result is widely varying standards and processes".

CIMA also calls for a distinction between non-executive directors and independent directors who have been selected on the basis that they have no conflicts of interest and independence of spirit and judgement. There should be a stringent recruitment process for chairmen and limited liability for *all* directors in cases where due process and diligence have been observed.

CIMA believes that, to widen the pool of potential independent directors, the risk-reward ratio needs to be adjusted. This does not mean paying them more "as this can create a conflict of interest in itself". Instead, CIMA argues in favour of capped liability for all directors where they can show they have followed due process and diligence and not acted fraudulently or negligently.

ICAEW

The main accountancy institute says that people from the accounting and legal professions are "obvious candidates" to widen the pool of non-executive directors, as are talented people below board level in the FTSE-350, in government and not-for-profit sectors. "Helping individuals to obtain their first post as a non-exec could be useful for both parties," the ICAEW says.

The ICAEW calls for a solution that preserves the integrity of the unitary board but which limits the amount of liability assigned to individual non-execs. It accepts the view of the Company Law Review that there should be no distinction between the legal *duties* of executive and non-executive directors, as this would undermine the unitary board concept. But it calls for some form of protection of non-executive directors' *liability*.

Andrew Sawers.

www.financialdirector.co.uk/briefing

Useful links

Websites for organisations referred to are:

- **www.napf.co.uk**
- **www.uksip.co.uk**
- **www.treasurers.org**
- **www.cima.org.uk**
- **www.icaew.co.uk**
- **The Higgs consultation paper is at www.dti.gov.uk/cld/non_exec_review/condoc.pdf**