The boards of quoted companies

The main findings of a new study of company board structure, described in this article, are:

- *The trend towards an increasing number of non-executive directors on the boards of quoted companies has been maintained: only one quoted company in twenty in the present study had no non-executive directors and, on average, one director in three was non-executive. Moreover, in 60% of the companies examined, the board included three or more non-executive directors; in 1979 this was true of only half the quoted companies.*
- *Almost one in three non-executive directors identified in this study was either a former executive of the company or a professional adviser to it. Roughly three companies in five had appointed such people as non-executive directors and they formed almost a half of the non-executives on the boards of these companies.*
- *Eighty-five per cent of the non-executive directors were receiving fees of £10,000 or less.*
- *Few companies provide information about the experience and qualifications of non-executive directors or the responsibilities of executive directors in their reports and accounts. Indeed, only one in two of the largest 250 industrial companies indicated in their annual reports whether directors were executive or non-executive.*

The March 1983 *Bulletin* reported the results of an investigation into the size and composition of the boards of companies in the *Times 1,000* list.[1] That article highlighted changes in the composition of company boards in the three years to 1982, and reported evidence that a growing number of companies, especially quoted companies, were appointing non-executive directors to their boards. To gauge whether this trend has been maintained, a fresh study of company board structures has now been undertaken.

In addition, as a related exercise, the reports and accounts of the largest 250 companies in the *Times 1,000* list have been examined to ascertain how much information is published about the qualifications and experience of directors.

Information provided by companies on their boards

The quality of a company's chief executive and board of directors has an important bearing on its performance. Companies, however, are not required either by law or, in the case of quoted companies, by The Stock Exchange to disclose details of the functions, skills or experience of board members to their shareholders and others whose livelihoods depend on the company's performance.

The main published source of information on a company's affairs, its annual report and accounts, has by law to name directors, indicate their remuneration and show their financial interests in the company and its subsidiaries. In addition, every company has to maintain registers of its directors, of their interests and those of their immediate families in the shares and debentures of the company, and of directors' service contracts. The first two registers may be inspected by members of the public, but the register of service contracts is required to be open only to members of the company. Listed companies must in addition meet the requirements of The Stock Exchange on disclosure of information about their affairs, but, as regards information on directors, these are only slightly more onerous than the law requires of all companies. When a company seeks a listing, for example, its directors must indicate their functions and their outside business interests where these have a bearing on the company's activities, as well as personal particulars. There is, however, no continuing requirement for listed companies to provide shareholders with information about the qualifications, experience and duties of directors.

An examination of the reports and accounts of the top 250 companies in the *Times 1000* list showed that only a minority of these companies disclosed more information about their boards than is required by law:

- 48% indicated which directors were non-executive;
- 24% described executive directors' responsibilities (apart from merely identifying the Chairman and Deputy Chairman);

(1) 'The composition of company boards in 1982': March 1983 *Bulletin*, page 66.

- 13% provided biographical information on non-executive directors, such as principal occupation and other directorships;
- 6% gave details of their audit committee and 2% gave the membership of other board committees.

The implication of these findings is that companies' reports and accounts are in most cases a poor guide to the range of skills and breadth of experience of company boards. This has significance not just for existing and prospective shareholders, but ultimately for the efficient working of the capital markets.

An examination of boards of quoted companies

In early 1983, the Bank wrote to the companies in the *Times 1000* list of the largest industrial companies in the United Kingdom, and the article in the March 1983 *Bulletin* describing the composition of company boards in 1979 and 1982 was based on replies from some 700 of these companies. The present investigation was confined to quoted companies (including companies on the unlisted securities market) in the *Times 1,000* list. There were two reasons for this. First, non-executive directors probably have a larger role to play in quoted companies, which are characterised by a wide spread of shareholders, few of whom, if any, will be involved in executive management. There is consequently a special need for independent directors on the boards of companies whose shares are publicly traded to monitor the performance of executive management.

The second reason for confining the study to quoted companies was more prosaic, reflecting the difficulty experienced in 1983 in determining the precise status of directors on the boards of subsidiary companies. Many non-executive directors on subsidiary boards are, for example, full-time directors or employees of either the parent company or other subsidiaries, and their role is not wholly comparable with that of an independent non-executive director of a holding company.

The study was also limited to quoted companies which responded to the 1983 survey and for which details of board size and composition in 1979 and 1982 were consequently available—a total of 410 companies. Although the coverage of this study was narrower than in 1983, its scope was wider. The 1983 investigation was confined to asking about board size and numbers of non-executives, but the opportunity has been taken on this occasion to ask also about the remuneration of non-executive directors and whether they were serving or had served the company in other capacities. Some 84% of the questionnaires that were sent out have been returned.

Because the investigation was confined to the largest quoted companies, the results may be thought indicative of best rather than typical practice regarding the appointment of non-executive directors, and, in particular, may not be representative of smaller companies. This possibility should be borne in mind when interpreting the findings; but it is worth pointing out that, on average, the larger companies in the study did not have a higher ratio of non-executive to executive directors than the smaller companies.

Table A
Board size and numbers of non-executive directors
Number of companies; *percentages in italics*

	Non-executive directors						
	0	1	2	3–5	6+	Total	
Board size							
3–5	10	14	8	3	—	35	*10*
6–8	7	18	43	63	1	132	*38*
9–11	2	8	15	63	17	105	*31*
12–14	1	—	4	27	21	53	*15*
15+	1	—	2	10	6	19	*6*
Total	**21**	**40**	**72**	**166**	**45**	**344**	*100*
	6	*12*	*21*	*48*	*13*	*100*	

Table A provides details of the sizes of the boards of the companies which returned questionnaires and of the numbers of non-executives on their boards. Company boards varied in size from three to twenty, but 132 companies (38% of those responding) had boards of between six and eight members and a further 105 (31%) had boards of nine to eleven members. At the extremes, one company in ten operated with a board of three to five directors and a slightly smaller number had boards of fifteen or more. As regards numbers of non-executive directors, there was, as with board size, a considerable diversity. 133 companies—almost two in five of those responding—had fewer than three non-executives on their boards, with 21 companies (6%) having none and a further 40 (12%) only a single non-executive. Almost half of those responding (166 companies) had between three and five non-executives on their boards, and a further 45 (13%) had six or more. There was, not surprisingly, a distinct correlation between the size of a company's board and the number of non-executive directors on it.

The average company in the study had a board with nine members, of whom three were non-executive (Table B). There did not, however, seem to be a simple relationship between board size and the ratio of executive to

Table B
Board composition classified by size of board and size of company
Number of directors; *percentages in italics*

	Numbers of directors					
	3–5	6–8	9–11	12–14	15+	All companies
Times 1000 companies (344 replies)						
Average board size	4.7	7.1	9.8	12.7	16.2	9.0
Non-executive directors:						
Average number	1.1	2.4	3.7	4.9	4.6	3.2
Percentage	*25*	*35*	*38*	*39*	*29*	*35*
Times top 250 companies (130 replies)						
Average board size	5	7.3	10.0	12.8	16.4	11.1
Non executive directors:						
Average number	2	2.3	3.8	4.7	4.6	3.9
Percentage	*40*	*32*	*38*	*36*	*28*	*35*
Times bottom 750 companies (214 replies)						
Average board size	4.6	7.0	9.6	12.0	15.3	7.7
Non-executive directors:						
Average number	1.1	2.5	3.6	5.9	4.7	2.8
Percentage	*24*	*35*	*38*	*49*	*30*	*36*

non-executive directors. Companies with the smallest and largest boards had the lowest proportions of non-executive directors—only one director in four was non-executive —whereas, for the bulk of companies with boards of between six and fourteen members, the ratio was better than one in three.

Information on board size and composition is shown separately for companies in the study in the top 250 positions of the *Times 1000* list and for those in the bottom 750 positions. Larger companies tended to have larger boards—the average 'top 250' company had eleven members against fewer than eight for the average 'bottom 750' company. There was little difference in the ratio of non-executive to executive directors.

Table C
Proportion of non-executive directors on company boards

Non-executive directors as percentage of board	Numbers of companies	Percent of responding companies
0–10	23(a)	7
11–20	34	10
21–30	72	21
31–40	81	23
41–50	57	17
51–60	51	15
61–70	16	5
71–80	5	1
81–90	5	1
91–100	—	—
	344	100

(a) Of which, 21 had no non-executives.

Table C shows how prominent non-executive directors are as a group on the boards of the companies studied. It shows that, while non-executives comprised on average 35% of the company boards, there was a considerable dispersion. For three in five of the companies, non-executives accounted for between 20% and 50% of their boards. Only one company in five had boards with a majority of non-executives.

The results of the 1985 study are compared with those for the same companies in the 1983 study (which related to 1979 and 1982) in Table D. This suggests that non-executive directors have become more numerous: only 6% of the companies had no non-executives on their boards in 1985, against 8% in 1982 and 14% in 1979. There has also been a steady increase in the percentage of

Table D
Comparison with the 1983 study

Number of non-executive directors	1983 study: results for quoted companies 1979	1982	1985
	Percentage of companies		
6 or more	11	13	13
3–5	41	43	48
2	22	22	21
1	12	14	12
0	14	8	6
	100	100	100
Average size of board	9.8	9.4	9.0
Non-executive directors:			
Average number	3.0	3.1	3.2
Percentage of total board	30	33	35

companies reporting three or more non-executives on their boards. In addition, there has been a trend towards smaller boards since 1979, with the reduction being attributable entirely to falls in numbers of executive directors. The number of non-executive directors on a typical board has in contrast increased slightly, so that they now form a slightly larger proportion of company boards than in 1979 and 1982.

A non-executive director must be capable of taking an objective view of the policies being advanced and followed by executive management if he is to fulfill his responsibilities to a company's shareholders. This means that a non-executive director's judgement should not be influenced by considerations stemming from financial dependence on the company or strong personal links with its executive management. To provide an idea of the numbers of non-executive directors who might face serious conflicts of interest, companies were asked to indicate how many of their non-executive directors were serving or had served the company in a professional capacity and how many were former executives of the company or its subsidiaries. The responses to this question are summarised in Table E. It shows that 209 companies—three in five of those in the study—had appointed professional advisers or former executives as non-executive directors: such directors accounted for nearly one in two of the non-executive directors of these companies and roughly one in three of all the non-executive directors covered. Within this group of 209 companies, 51 (roughly one in seven of the companies in the study) had looked to both professional advisers and former executives to serve as non-executive directors.

Table E
Non-executive directors who are former executives or have professional connection
Number of directors

	Companies with non-executive directors: Having professional relationship only	Former executives only	In both categories	In neither category	Total
Non-executive directors:					
With professional relationship	116	—	57	—	173
Former executives	—	105	68	—	173
Others	173	178	65	338	754
Total	289	283	190	338	1,100
Executive directors	541	375	260	827	2,003
Total directors	**830**	**658**	**450**	**1,165**	**3,103**
Number of companies	*93*	*65*	*51*	*135*	*344*

It is important that, as well as being independent of executive management, non-executive directors should not be constrained by financial considerations from pressing their view, if necessary to the point of resignation. This means that they should not be dependent on their remuneration as a non-executive director of a particular company for a sizable part of their income. Though the study did not attempt to assess the degree of financial independence enjoyed by non-executive directors, it did include a question about

Table F
Remuneration of non-executive directors
Percentage of companies

	Up to £2,500	£2,501–£5,000	£5,001–£7,500	£7,501–£10,000	Over £10,000	Total
Top 250 companies	3	9	36	31	21	100
Bottom 750 companies	9	28	40	13	10	100
All companies	**6**	**19**	**39**	**21**	**15**	**100**

their basic fees. Most non-executive directors are paid quite modest fees, but a sizable minority—15%—receive a basic fee of more than £10,000 (Table F). Larger companies pay their non-executive directors more than smaller companies. These findings, however, almost certainly understate non-executive directors' total remuneration, since, apart from benefits in kind, it is common for them to receive additional fees for special duties—for example if they serve as chairman or deputy chairman—and for ad hoc consultancy.

Some issues that are raised

The results of the studies of company board structures and of information about directors in companies' reports and accounts raise several issues that deserve further consideration. The first concerns the pace at which companies are appointing non-executive directors to their boards. The study of company boards provides evidence that more quoted companies are appointing non-executives to their boards and that non-executives are forming a larger proportion of boards. But it also shows that two in five companies had fewer than three non-executives on their boards and only one company in five had boards with more non-executives than executives. Moreover, the study provides no evidence that the trend towards greater use of non-executive directors is gathering pace. These findings raise some doubts about the adequacy of the current approach, based on argument and persuasion, towards extending the use of non-executive directors on company boards in this country.[1]

While numbers are obviously relevant, it is equally if not more important for the shareholders of a company that its non-executive directors should be suitably experienced and have the right personal characteristics to be effective. Non-executive directors should, in particular, be independent of a company's executive management, or at least able to take a detached view of the policies being advanced by them. The study of the boards of the largest quoted companies showed, however, that a majority of companies had looked to former executives and professional advisers to serve as non-executive directors. This is not surprising, because such people are well known to the chairman and directors of a company and their knowledge of the company's affairs allows them to make an immediate contribution to board discussions. However, it is perhaps disquieting that at least one in three of the non-executive directors identified in this study was serving or had served their companies in another capacity, since these people may find it hard on occasions to exercise the independence and objectivity required of a non-executive director.

A third issue, raised by the examination of company reports and accounts, concerns the adequacy of information published by companies about their boards. A majority of the largest 250 industrial companies published only the minimum information required by law. Clearly shareholders would be better able to form an assessment of boards of directors if companies were to publish more information about the qualifications, experience and responsibilities of their directors. How this should be achieved—whether by pressure from shareholders, by Stock Exchange requirement (in the case of quoted companies), or by legislation—is a matter for further debate.

(1) This approach is typified by the activities of PRO NED, a body set up by the Bank and other interested bodies to promote the appointment of non-executive directors and to offer a placement service for companies seeking to make such appointments.