



THE GIBRALTAR
INSURANCE INSTITUTE

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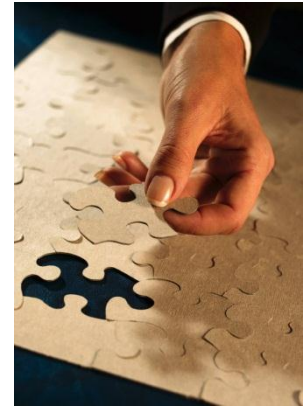
R.P.S. Business Consultancy Ltd



Non-Executive Directors

Regulatory Interference or

Invaluable Piece in the Governance Jigsaw?



Agenda

- Why are NED roles growing in importance?
- Types of NED
- What does this really mean?
- Fit of NEDs into organisations
- NEDs – necessary but not sufficient??
- NEDs – part of a much bigger picture
- Questions





Why are NED roles growing in importance?

LEMMA EUROPE
insurance company limited



- Financial crisis driven – business failures
- Firms that failed evidenced one of more of the following:
 - Dysfunctional board
 - Domineering CEO (not untypical in small entrepreneurial and owner managed businesses i.e. their money invested)
 - Key posts held by individuals without required technical competence (right place-right time scenario)
 - Inadequate “four-eyes” oversight of risk
 - Inadequate understanding of aggregation of risk
- Lack of, inadequate or ineffective corporate governance structures
- NED role is pivotal in ensuring active governance of the firm
- NED definition(FSA):
 - **“ a director who has no responsibility for implementing the decisions or the policies of the governing body of a firm”**

Types of NED

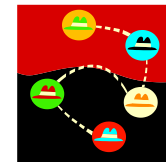


- “Stakeholder” NEDs and Independent NEDs
- “Stakeholder” NEDs:
 - Engaged in another capacity or linked to the company - e.g. legal advisors, audit, shareholder grouping, parent company etc.
 - Will clearly support the group they represent
 - May have financial ties and commercial relationships that could influence their judgement
- Independent NEDs:
 - Not an employee of same company or same group
 - Not a shareholder of same company or group
 - Not a supplier or customer to the company
 - No family connection with the business
 - Fixed term of directorship (usually 3 years) and therefore less likely to be motivated by self-preservation when making decisions
 - Not so heavily dependent on NED remuneration as to make resignation difficult
- There is a place for both types of NED and a clear need for independent NEDs



What does an independent NED need to be and do?

- Independent(!)
- Impartial
- Wide experience
- Specialist knowledge
- Personal qualities:
 - Integrity and high ethical standards
 - Sound judgement and enquiring mind:
 - Question intelligently
 - Debate constructively
 - Challenge rigorously
 - Decide dispassionately
- Independent NED's ability to provide a credible challenge to the business and role of Board in setting "culture" and "tone from the top" is key
- Higgs Report states that the role of the NED has:
- **"...two principal components: monitoring executive activity and contributing to the development of strategy."**



What should an independent NED do before accepting a position?

- Before taking up an NED position they should assure themselves that:
 - Company has effective board led by suitable CEO and Chair with support of appropriately qualified directors
 - Board has established processes for making strategic decisions
 - Company is compliant with all legal requirements
 - Sound and well established systems for risk management and internal control exist
 - Effective accounting and audit procedures are in place
 - Company is compliant with all reporting requirements
 - Corporate governance procedures are in place to ensure best practice
- Companies who are serious about independent NED appointments will produce information packs outlining the above
- Companies should also undertake a rigorous interview process to establish candidates' credibility for an NED position



Independent NED needs and responsibilities after accepting a position

- Signed contract outlining role, responsibilities, duration, termination etc.
- Suitable induction and familiarisation training
 - Sufficient to provide a good working knowledge of the firm
 - Emphasis on strategic and corporate governance issues
- Likely to chair board committees – e.g. Investment/Audit/Risk/Compliance -underlining independence
- Possible oversight on remuneration issues
- Prepares for, attends and plays an active part in board and other committee meetings (!)
- Will commit to additional time beyond board meetings to maintain knowledge of company
- Acts as the conscience of the Executive Team
- Challenges to ensure Board takes a robust and evidential approach – not just to be a pain!!
- NEDs should be best placed to ask the critical questions of the Board
- Seeks re-assurance that appropriate and effective corporate governance is in place
- Where an executive team appears to be making a number of errors regulatory focus will swing on to the role of the NEDs - what are they doing to ensure that appropriate governance is in place and working?
- **NEDs as culpable as other directors in the event of regulatory censure or failure**
- Remuneration should adequately reflect role and responsibilities



Can or should you manage without an independent NED?

- What are you really trying to achieve here?
 - Independent overview of corporate governance
 - Independent challenge of proposed strategy
 - Independent challenge of significant investment
 - Independent challenge of capital adequacy
 - Independent challenge of dividend strategy
- Possible to use independent advisors and consultants
 - Potential cost implications
 - No formal director responsibilities
 - Possible but not easy – potential for small firms?
- If NED positions are limited to locally based directors this will severely restrict the skills pot and independence
- Nature of ownership will influence the options
- Independent NED option – not limited to local – may be the best fit

NEDs – Next Steps

- Take a dispassionate view of your Board composition
 - Is there independent and effective challenge?
- Will the company benefit from an independent NED?
- Proportionality is key
- If yes, undertake professional and structured recruitment process for an independent NED
- If no, continue to review the position
 - circumstances change!

NEDs – necessary but not sufficient

The bigger picture



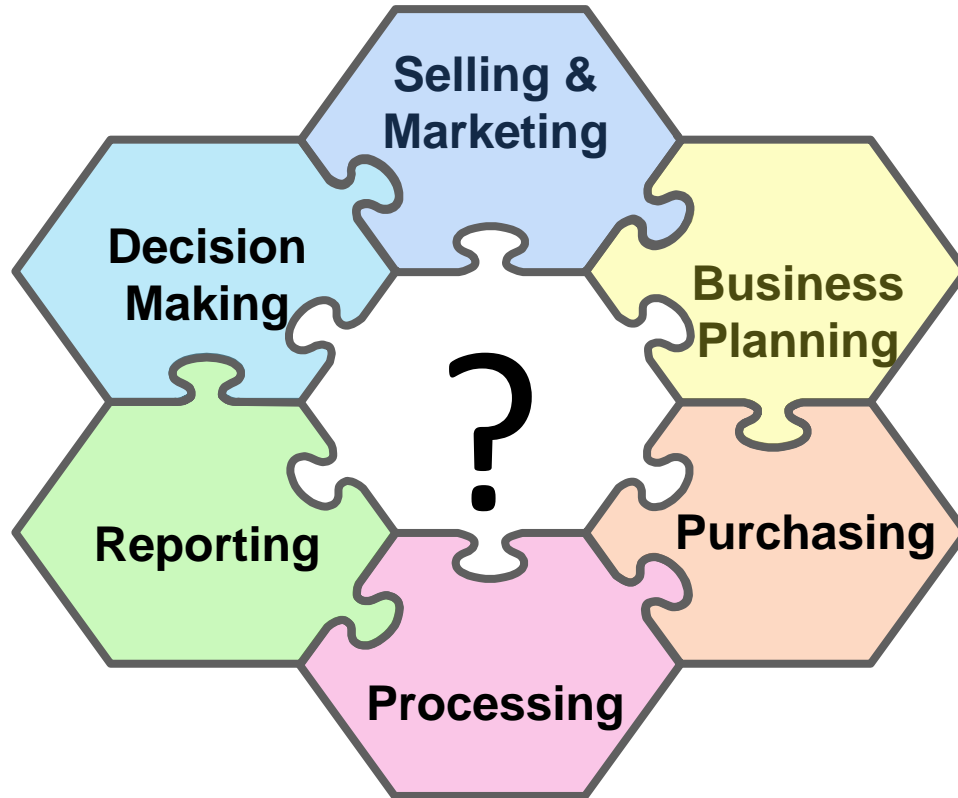
- NEDs are part of the corporate governance structure of the firm
 - Key decision making groups
 - Group and individual authorities
 - Risk assessment and management
 - Compliance and audit activities
- All backed by an evidential approach
- All supporting a business aimed at delivering its business plan - and profit – in the most efficient and effective manner possible – and at least risk
- Size and nature of the firm will determine the way in which these activities are delivered
- NEDs have a clear role within this structure to ensure the executive implement and maintain their firm’s corporate governance structure
- Cadbury Report:
 - **“...the calibre of the non executive members of the board is of special importance in setting and maintaining standards of corporate governance”**

Overall Corporate Governance picture

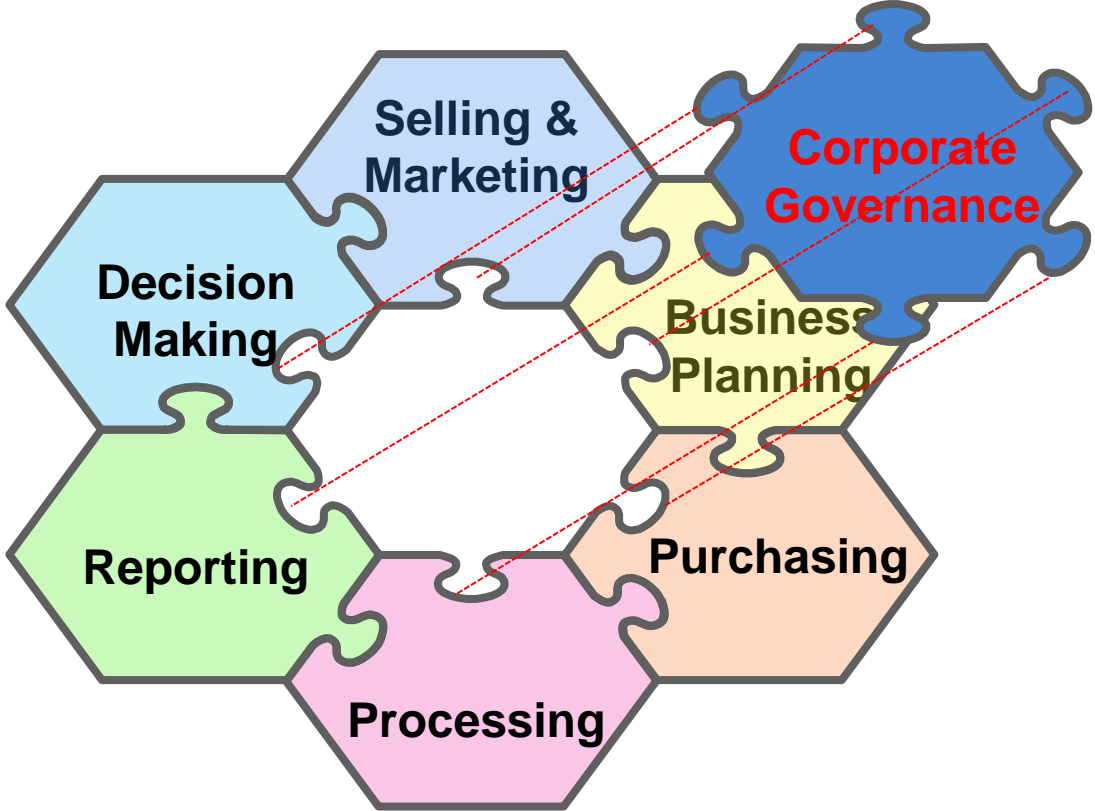
- Why?
 - Key to running efficient and effective operations in support of your business plans
 - Will act as an early warning if results do not reflect plans
 - Will also leave you very well placed when Solvency II finally arrives!
 - (NB most of this is something you should already be doing anyway!!)



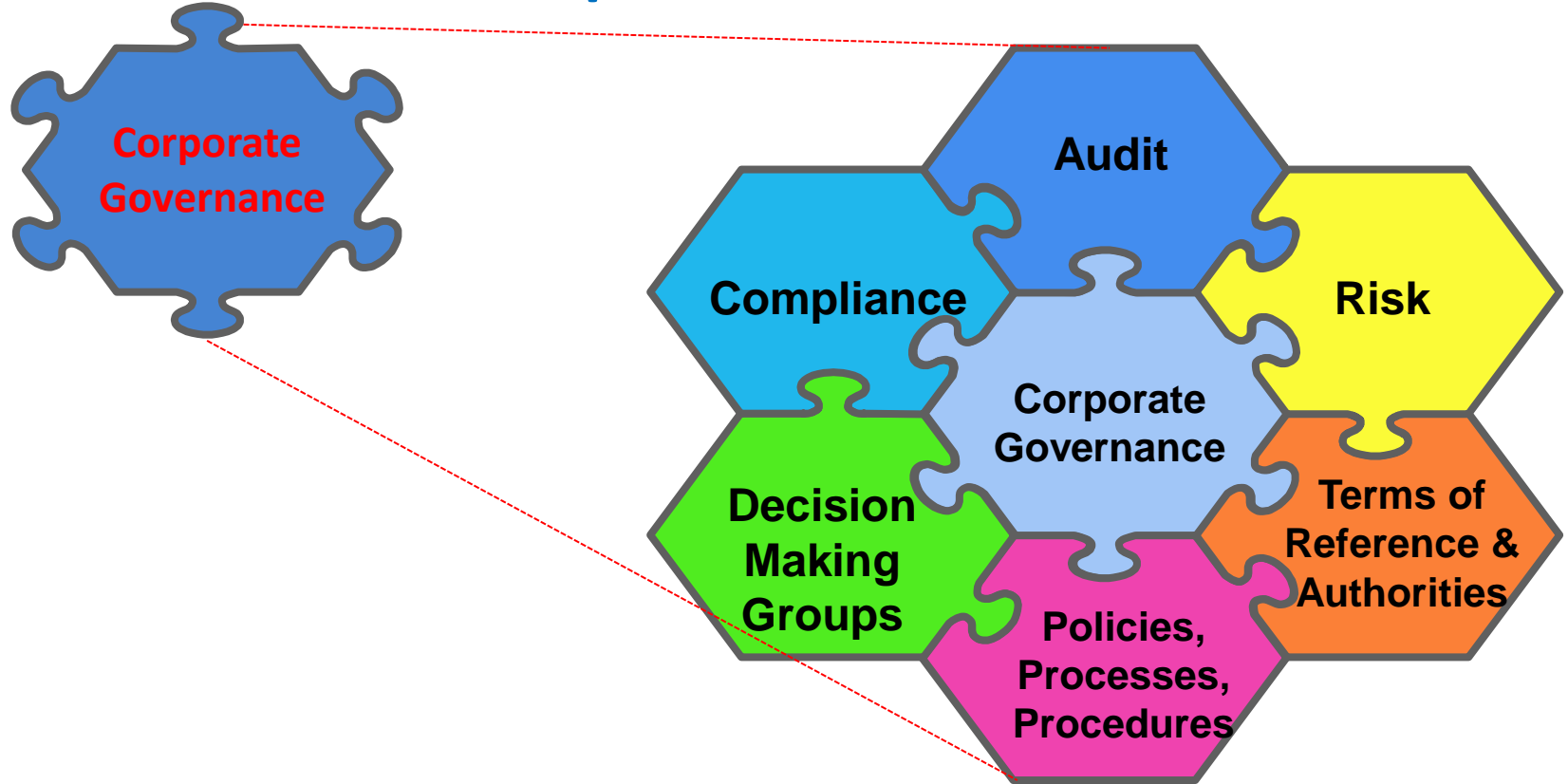
The Missing Link...



The Right Fit For Your Business



The Complete Business



Corporate Governance

- Means of controlling the organisation
- Acts as fulcrum for all other activities
- Consistency of approach
- No surprises



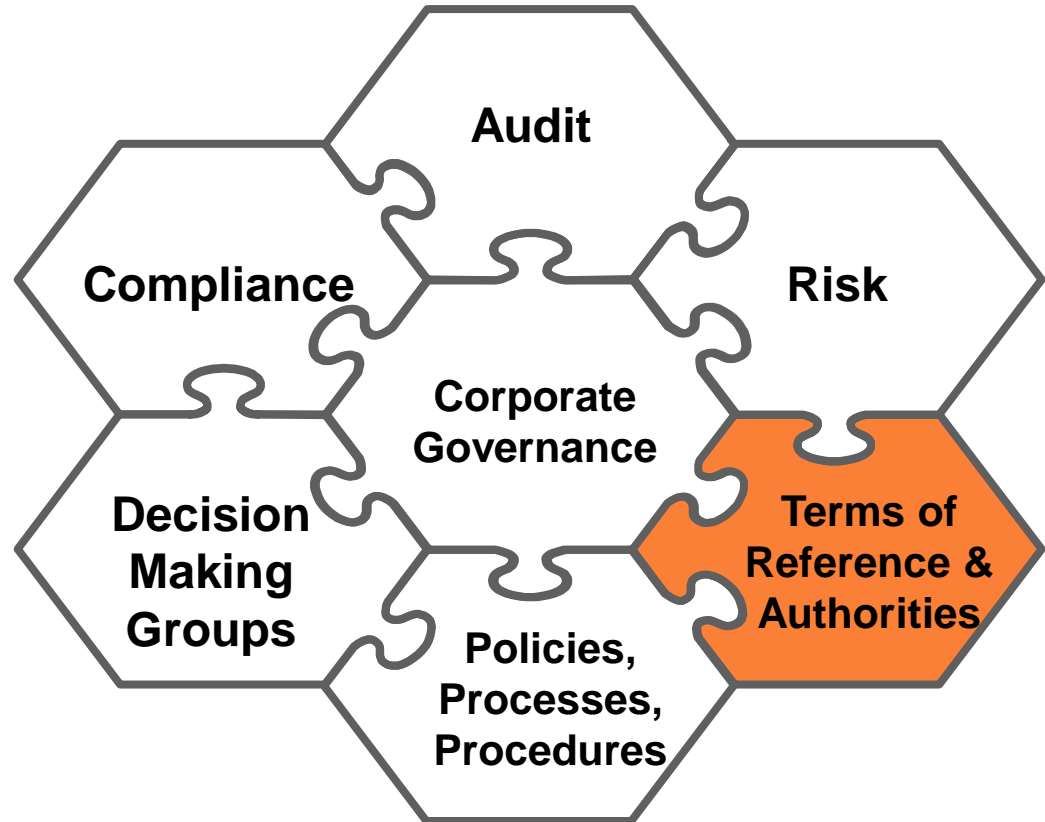
Decision Making Groups

- Key means of controlling operations
- Terms of Reference
- Responsibilities
- Authorities
- Membership
- Reporting lines
- Interlocking meeting schedules



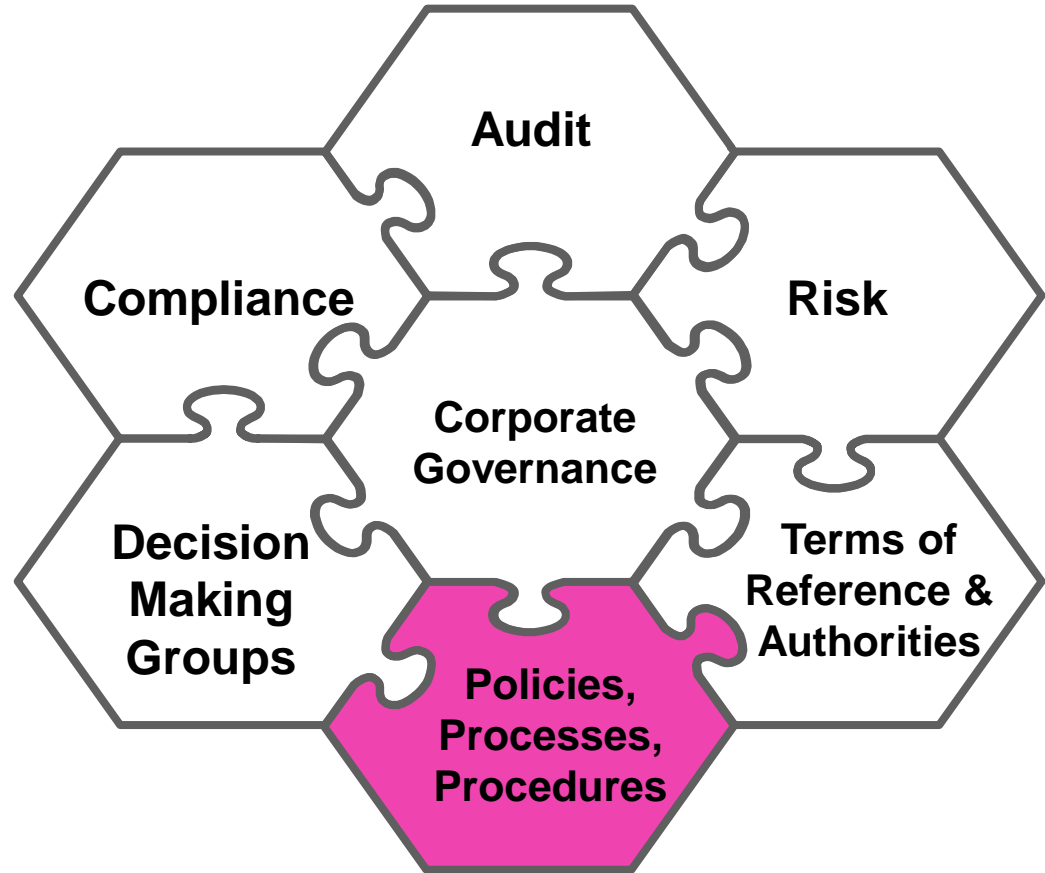
Terms of Reference and Authorities

- Define purpose of each decision making group
- Draws attention to any legal or regulatory requirements
- Ensures participation by all relevant stakeholders in subject matter
- Defines authority and reporting lines of the DMG
- Will also define all individual authorities and referral points



Policies, Processes and Procedures

- Defines standard organisation approaches
- Internal and external dimensions
- Some documentation requires overt employee and third party acknowledgement
- Defines organisation business processes and procedures
- Formal basis to define support requirements (e.g. technology and resource skill sets)



Compliance

- Defines regulatory parameters and applicable rules of operation
- Early warning for likely/impending regulatory changes
- Aligns with business plans alongside audit and risk functions
- Establishes compliance monitoring schedules
- Reports against regulatory requirements
- Remains flexible to inevitable business plan changes
- Acts as organisation focal point for compliance



Audit

- Independent and objective assurance activities
- Audit aligns to business, risk and compliance plans
- Establishes appropriate audit schedules
- Reports on audit against required standards
- Remains flexible to inevitable business plan changes
- Acts as organisation focal point for audit



Risk

- Responsible for risk approach and methodology
- Ensures risk assessments undertaken
- Responsible for risk register administration
- Supports determination of organisation's risk appetite
- Monitors and reports risk register rectification progress
- Establishes trigger points for risk assessments
 - Internal and external events
- Ensures risk management aligns with audit and compliance plans



Next Steps



- Consider how to fit into your organisation
- Independent NEDs can and should act as an effective catalyst where necessary
- Proportionality is key
- Will force you to understand how you do business!

Thank You for Listening

Questions?

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