The Role of the Non-executive Director: findings of an empirical investigation into the differences between listed and unlisted UK boards*

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This study, based on a comparison of the Combined Code Guidelines for non-executive directors between listed and unlisted boards, suggests that on unlisted boards non-executive directors have a greater degree of involvement in strategic development, financial monitoring, shareholder communication and overall board contribution than on listed boards, but a lesser degree of involvement in the monitoring of management, the setting of executive remuneration, the appointment and removal of executives, and succession planning. The importance of risk analysis and induction is considered high across both sectors, although board development and independence is considered less important on unlisted boards.

Keywords: Non-executive director, corporate governance, boards of directors, listed, unlisted, family company, venture capital

Introduction

Corporate governance

Attention to, and interest in, corporate governance, defined by Cadbury (1992) as the system by which companies are directed and controlled, has grown exponentially over the last three decades (Demirag and Solomon, 2003). Recent corporate governance reforms have affected UK boardrooms in a variety of ways, increasing the number of non-executive directors, addressing chairman/CEO duality and imposing age, term and compensation arrangements for directors (Daily *et al.*, 2003). Unlisted companies, i.e. companies which have unlisted shares and no access to equity capital markets (Modern Company Law, 2002), have not yet attracted the attention of the regulators, even though they constitute the vast majority of companies in the UK. Many unlisted companies are as large and complex as their PLC counterparts, and are often run by professional executives who have been charged with the task of competing successfully with listed companies but without access to equity funding. However, in spite of the difficulties it appears that unlisted companies are becoming more interesting for those shareholders who prefer to concentrate on performance and long-term growth rather than short-term profit (Waine, 2002).

Unlisted companies differ from listed companies in a variety of ways. Externally they operate without attracting institutional interest, scrutiny from the regulators and attention from the media. Internally they concentrate on cashflow rather than reported earnings, their

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boards of directors often have a real financial interest in the business and they have minimal concerns about the current shareholder value of the enterprise (Gottesman, 2003). Unlisted companies also have different governance issues. In family companies fortunes are linked, and there is a strong incentive to align executives and minimise agency issues (Cannella and Monroe, 1997). Family companies often suffer severe disadvantages compared with their PLC counterparts; wealth is not usually diversified across a portfolio of interests, and it is more difficult for family companies to undertake high risk/high return projects (Cannella and Monroe, 1997). Furthermore, executive management positions are often limited to family members, restricting the labour pool and potentially excluding qualified and capable talent (Anderson and Reeb, 2003). In venture capital (VC) backed companies there are additional complexities. Venture capital ownership results in a dramatic exchange of power from executive shareholders to external shareholders (Lynall *et al.*, 2003) and companies are often at a different, and more turbulent, stage of the lifecycle (Lynall *et al.*, 2003).

Partly due to their inaccessibility there has been very little research on the involvement of non-executive directors on unlisted boards, and no comparison of the role across sectors, even though the normative prescriptions and empirical results from large listed company studies may be inappropriate (Ford, 1988; Daily and Dalton, 1992, 1993).

The role of the non-executive director

In order to understand more about board behaviour and dynamics, we need to identify the behaviour of individual directors (McNulty and Pettigrew, 1999), and the direct and indirect influences on their effectiveness and involvement. The role of the non-executive director is often described as that of a long-term, consensus-based decision maker (Tricker, 1978; ProNed, 1992), and as a custodian of the governance process (Higgs, 2003). Although the terminology varies three main roles have been identified; control, service and resource dependency (Johnson *et al.*, 1996).

The literature indicates that the involvement of non-executive directors on unlisted boards may be very different to that on listed boards (Whisler, 1988; Forbes and Milliken, 1999; Fiegener *et al.*, 2000), partly due to contingent factors such as the ownership structure and the power between internal and external stakeholders which affects the composition and function of the board (Fiegener *et al.*, 2000; Gabrielsson and Huse, 2002). The control role is diluted due to the lack of separation of ownership and control (Forbes and Milliken, 1999; Deakins *et al.*, 2000b), and the service and resource roles are increased due to company lifecycle (Huse, 1990; Daily and Dalton, 1992, 1993; Randoy and Goel, 2003). The role is suggested to have increased breadth and depth; the provision of non-executive counsel and expertise (Whisler, 1988), knowledge and skills (Huse, 1990) and external relationships (Borch and Huse, 1993) are all suggested to be of great importance to the unlisted company (Dyer, 1986; Nelton, 1987; Whisler, 1988), supporting those theories which focus on the supply of resources and social networks.

The research programme

This research, set within the context of both UK listed and large unlisted companies, was conducted through a series of semi-structured in-depth interviews with non-executive directors serving simultaneously on listed and unlisted boards. The research questions investigated were:

- How do the roles and responsibilities of non-executive directors serving on FTSE 100 or 250 boards differ from those serving on unlisted company boards?
- Do the Combined Code Guidelines (FRC, 2003) for non-executive directors have relevance to non-executive directors serving on unlisted company boards?
- How do these findings contribute to and influence board theory?

Board research studies are often quantitative in focus, based on demography (Gabrielsson and Huse, 2002), archival data and hypotheses testing deduced from board theory perspectives which have limited relevance for the practitioner. In order to appreciate the multiple perspectives involved with perceptions of governance and board behaviour this research was conducted adopting an interpretive approach, carefully structured in order to maintain reliability and validity of method.

The scope of research was limited to those non-executive directors serving on the boards of both a FTSE 100 or 250 company, and a large unlisted company (i.e. family or VC-backed companies) with either a minimum turnover of £10m per annum or more than 100 employees, and investigated the roles of strategy, financial monitoring and risk analysis, performance monitoring, executive remuneration, appointing and removing directors, succession planning, induction and development, shareholder communication, independence and overall board contribution.

Table 1: Definition of measurement

Low	One to five respondents noted a high involvement or value
Low–medium	Six to ten respondents noted a high involvement or value
Medium	Eleven to fifteen respondents noted a high involvement or value
Medium–high	Sixteen to twenty respondents noted a high involvement or value
High	Twenty-one to twenty-five respondents noted a high involvement or value

Method

Sample

It is difficult to define the population of non-executive directors serving on both listed and unlisted company boards due to the limited statistics available on unlisted companies (Kelly *et al.*, 2000; Westhead *et al.*, 2002). In 2002, as part of the Higgs (2003) review, research was undertaken to build a factual picture of the current population of non-executive directors serving on UK listed boards. From a total population of 3908 individuals holding non-executive directorships in UK listed companies at that time, 80 per cent were holding only one post, leaving 782 individuals holding more than one non-executive post (Higgs, 2003). Within these limitations this research assumed that the population relevant to this study was expected to comprise of between a minimum of 10 per cent (78) and a maximum of 20 per cent (156) non-executive directors currently serving on a FTSE 100 or 250 company board and a large unlisted company board.

Although this research sample was not random, the respondents had a wide range of corporate experiences, and the companies represented were widely diversified, many with substantial international businesses and subsidiaries, and complex internal structures. The gender representation was 84 per cent male, 16 per cent female, with an average age of 58.1 years, and 28 per cent holding an honorary title. Each of the respondents represented an average of 3.0 listed companies and 3.4 unlisted companies. In total, 74 listed companies and 86 unlisted companies were represented; 44 per cent of respondents had specific experience of family companies, 28 per cent of respondents had specific experience of VC-backed companies, and 72 per cent of respondents described themselves as professional non-executive directors or pluralists.

Procedure

The one-to-one interviews, which were first conducted as a pilot study of 10 respondents followed by a further 15, were semi-structured, allowing the respondents the ability to talk freely and candidly about their roles and responsibilities within a limited time frame (usually an hour). The interviews were recorded on minidisc and transcribed word-for-word before being coded manually and through specialised software in order to identify primary and secondary codes. The respondents were promised complete anonymity and confidentiality, and all specific references were removed from the final transcriptions.

Analysis

ATLASti 5.0, a personal-computer programme developed for the support of text interpretation (Muhr, 1991), was used for collating the transcriptions and additional data, and for secondary coding; the coding process identified over 50 major themes, after which the data was interpreted and modelled. Data collection and analysis was conducted in tandem, starting with the pilot data, and written up continuously through the research programme. Levels of involvement and value were measured using the scale shown in Table 1, analysed within the context of corporate lifecycle, structure, culture and process, and interpreted within the context of the non-executive role and its theoretical implications.

Research findings

This paper offers a snapshot of the research findings. Data from 25 respondents indicates that non-executive directors serving on unlisted boards have a greater involvement in strategy, financial monitoring, shareholder communication, and overall board contribution, and a lesser involvement in management monitoring, executive remuneration, appointing and removing directors, and succession planning than on a listed board. The processes of risk analysis and induction are both considered to be of great importance across both sectors, and the relevance of board development and independence, both structural and philosophical, are considered to be less important on unlisted boards than listed boards. These results are illustrated in Figure 1.

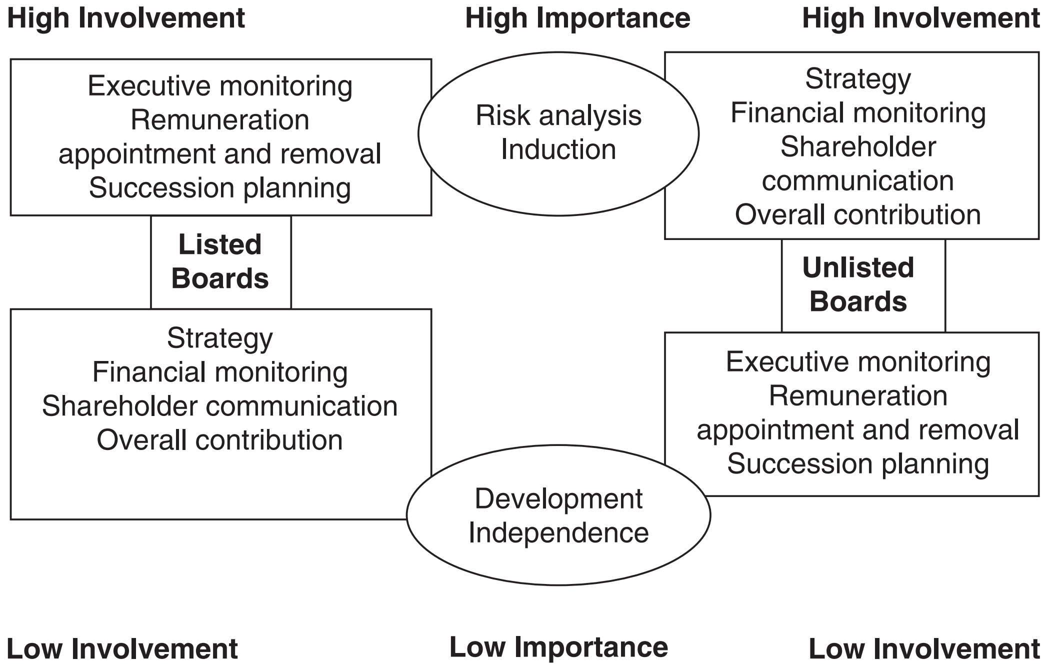

Figure 1: Summary of research findings

Areas of greater involvement on unlisted boards

Non-executive directors serving on unlisted boards have a greater level of involvement in strategy, financial monitoring, shareholder communication and overall board contribution than on listed boards. Due to the differences in lifecycle, structure, culture and process between listed and unlisted companies, non-executives benefit from closer relationships with both executives and shareholders, familiarity with company operations, lack of external scrutiny and isomorphic pressure, and encouragement from all constituencies to play a wider role.

Involvement in strategy

Strategic process does not operate in a vacuum; every company is influenced by certain factors which affect and constrain its strategic options (Stiles, 1998). The role of the non-executive director is influenced by a variety of internal and external factors (McNulty and Pettigrew, 1999), including the frequency and formality of discussion, company lifecycle and complexity, external visibility and internal presentation. In contrast to the FRC guideline, it appears that non-executive directors have a limited role in strategy development on listed boards; strategy sessions are infrequent and executive-led, often planned as annual or bi-annual events (McNulty *et al.*, 2002), a format which has not changed since the early 1990s (Pye, 2000). Board contribution is prejudiced by information asymmetry; executives are motivated and incentivised by short-term results, and non-executives are unfamiliar with company operations and can only communicate through formal channels. Furthermore, strategic contribution is affected by external visibility and isomorphic pressure (Hawley, 1968), encouraging companies to think and act in similar ways regardless of their individual needs (DiMaggio and Powell, 1983; Bender, 2003a). Contrary to the suggestion that boards evolve from monitoring to strategic roles (Rindova, 1999), the opposite appears more common amongst respondents. This research suggests that there is ample opportunity for executives to undermine non-executive authority, and that an overemphasis on monitoring has prioritised the control role over strategic contribution. There are growing concerns over the dominance of corporate governance over the role of strategy, and the influence of additional bureaucracy in the boardroom. Within these limitations non-executives are asked to comment on, rather than contribute to, strategic development.

On unlisted boards non-executives have a greater involvement in strategic development. Executive teams are often less experienced, and shareholder agendas are transparent; non-executive directors readily align themselves with shareholders, managing disparate interests across shareholder groups in order to achieve common strategic goals. Decisions evolve through complex, non-linear and fragmented processes over time, and are conducted as a continuous debate. Research suggests that in order for a company to survive and prosper, it must remain flexible and responsive to changes in its own performance levels and to changes in its environment (Kisfalvi, 2000); this research indicates that unlisted companies are very sensitive to environmental changes, and suffer from fewer and less robust internal resources, encouraging non-executive directors to be more flexible, opportunistic and involved in their approach to strategic development than on a listed board. Agency issues are less visible, allowing non-executives a closer relationship with management and company operations.

Although familiarity with company operations, executives and shareholders allows non-executive directors greater power and influence over strategy, there are some limitations to the role; corporate lifecycle, ownership and culture regulate non-executive involvement. VC-backed companies have transparent exit plans which dominate their strategic horizons, and family companies often have longer-term views, more conscious of survival, harmony and employment opportunities than profitability and market position (Trostel and Nichols, 1982). Non-executive input is often designed to maintain a balance of boardroom views, and limit the influence of shareholder autonomy, rather than challenge and change strategic direction.

Involvement in financial monitoring

In listed companies internal resources are plentiful and financial teams are sophisticated. The frequency of structured meetings, and the preparation of financial information, have a positive impact on the performing of board functions and the fulfilment of legal responsibilities (Demb and Neubauer, 1992). However the literature recognises the potential for information asymmetry due to external pressure and executive self interest; management hegemony theory suggests that executives may be tempted to manage the presentation of financial information to the board (Brown, 2001; Matsumoto, 2001; Bartov *et al.*, 2002; Fields and Keys, 2003), facilitated by superior executive information on company operations and likely future performance (Langevoort, 2001).

This research suggests that although non-executives serving on listed boards are satisfied with the quality and presentation of financial information, and are aware of the significant internal resource that makes it possible, they operate at a significant distance from the sources of meaningful data. The formality of financial planning and its associated paperwork has increased the quantity of information given to non-executive directors, forcing them to rely heavily on executive interpretation and the satisfaction of the audit committee. There is considerable scope and incentive for earnings management, facilitated by corporate complexity and remuneration structures, which allows financial presentation to be executive-led and places additional demands on non-executive sophistication and understanding.

On unlisted boards non-executives have a greater involvement in the monitoring of financial information. Unlisted companies suffer from inconsistent information due to vague divisions of responsibilities, the absence of formal reporting systems (Gabrielsson and Winlund, 2000) and the lack of human resources (Daily and Dalton, 1993), rather than political manipulation. Informal communication channels allow non-executives the freedom to ask for detailed financial information in a direct way and to offer additional expertise; in many cases non-executives are themselves shareholders with easy access to financial data, and are often in a position to influence financial presentation. Furthermore, on VC-backed businesses investor representatives are continuously engaged in detailed and contractual financial monitoring, which is shared with other members of the board.

Involvement in shareholder communication

Although there has been significant attention paid to the rise of shareholder activism, and board-level accountability (Rindova, 1999), shareholder communication with non-executives directors of listed companies is extremely limited. Institutions have chosen not to interfere with management in the majority of cases, and executives remain largely unmonitored (Monks and Sykes, 2002); due to price sensitivity meetings are highly structured, involving only key board members at specified times in the year, and focusing mainly on high-level strategy and governance. This research suggests that although the views of shareholders, and their power to influence structure, have become increasingly obvious to respondents, shareholders do not have the time or inclination to communicate with non-executive directors during stable corporate conditions, who are in turn reluctant to expose themselves in an increasingly litigious environment.

In unlisted companies shareholder communication is a very different process. Shareholders are often present, either as executives and/or board members, and their agendas are transparent. There is no price-sensitive information that influences communication channels, and very little scrutiny from the external environment. Shareholders are often less fragmented in number and geography, and have much higher levels of informal communication with non-executive directors than their PLC counterparts. Although the blurring of roles between executives, non-executives and shareholders on unlisted boards facilitates a constant communication and information flow between the parties, it highlights the issues of shareholder dominance. Non-executive directors have far greater responsibilities for the protection of minority shareholders, who do not have the same voice and exit framework possibilities for expressing dissatisfaction (Hirschman, 1970), and have little protection against the autonomous wishes of dominant shareholder coalitions.

Overall board contribution

A common theme emerges from the literature; effective boards require capable individuals of high status (Ward, 1998), who are able to contribute large company experience, financial expertise and credibility with shareholders (Samuels *et al*., 1996). This research suggests that, due to non-executive distance from company operations, contribution on listed boards is expected to be generalised in nature and less specific about detailed operations and industry sectors. Attention and time dedicated to corporate governance has significantly increased over the last decade, influencing both the substance and the process of board discussion, and highlighting the control role of the board. Agency and management hegemony influences, and the potential for information asymmetry, have encouraged non-executives to focus on those issues relating to executive performance and alignment through formal and structured processes.

On unlisted boards there is no institutional requirement to appoint non-executive directors, and they are appointed by invitation only. Unlisted companies which have appointed non-executive directors have developed from the lifecycle stage where boards simply reflect the social networks of dominant power (Lynall *et al*., 2003), recognising an increased resource and legitimacy need from the board. Non-executive contribution is considered to be vital for aligning the interests of shareholders and executives, and for supporting enterprise; in order to fulfil the breadth and depth of role, non-executives are often expected to have a thorough and detailed understanding of the business and industry sector. Although the literature is inconclusive, there is evidence that larger boards limit the provision of strategic direction and performance (Baysinger and Hoskinson, 1990), and the ability to control management and protect shareholder interests (Cochran *et al*., 1985). Unlisted boards are often smaller, with fewer non-executive directors (Lorsch and MacIver, 1989; Demb and Neubauer, 1992; Dalton *et al*., 1999), meeting more frequently on an informal basis (Gabrielsson and Huse, 2002). This research supports the view that the size and composition of the board influences the quality of directors' deliberations and the level of overall contribution.

The literature also suggests that cross-fertilisation of ideas and experiences adds to non-executive contribution; research indicates that directors cross-reference innovative solutions and models between industries (Rindova, 1999). This research offers strong support for resource allocation and social network theory, revealing a breadth and depth of role far beyond that on a listed board. Non-executive directors supply unlisted companies with a wide range of experiences (Pfeffer and Salancik, 1978; Carpenter and Westphal, 2001), drawing on their functional backgrounds and international experiences (Fredman, 2002; Certo, 2003). Furthermore, they bring individual social capital and legitimacy through their personal networks and institutional affiliations (D'Aveni, 1990; D'Aveni and Kesner, 1993).

Areas of higher involvement on listed boards

This research suggests that non-executive directors on listed boards have a greater degree of involvement in the monitoring of management, the setting of executive remuneration, the appointment and removal of executives, and succession planning than on unlisted boards. Unfamiliarity with company operations, distance from management and clarity of expectation increase non-executive influence over executive structure and alignment. In contrast, familiarity with executives and company operations, increased executive sensitivities and the presence of dominant shareholders on unlisted boards reduces non-executive effectiveness in the area of people management.

Involvement in monitoring management performance

A legalistic approach suggests that listed boards do not monitor management performance in line with shareholder expectations

(Zahra and Pearce, 1989), partly due to the superior knowledge of the CEO (Lorsch and MacIver, 1989), and the part-time involvement of non-executive directors. Respondents acknowledge that they are operating at a significance distance from management, unable to spend sufficient amounts of time with executives, and suffering from information asymmetry, potentially giving management de facto control (Mace, 1971). Furthermore, they recognise that corporate performance is influenced by external and often unidentifiable factors which are outside management control (Walsh and Seward, 1990; Heslin and Donaldson, 1999). However, despite the difficulties, it is accepted that the non-executive role on a listed board encompasses the monitoring of management and performance, and is facilitated by the formality of structure and processes.

Non-executives on unlisted boards have a reduced need to monitor executives due to the lack of agency issues (Shleifer and Vishny, 1997; Randoy and Goel, 2003); personality traits and the natural chemistry between directors are suggested to be magnified (Deakins *et al.*, 2000a), and information asymmetry and opportunism is lessened through close working and personal relationships between executives and non-executives (Gabrielsson and Huse, 2002). Non-executive directors have a limited role to play; dominant shareholders determine executive objectives and are incentivised to monitor their process. Furthermore executives, often motivated in a different way and uncomfortable with the public pressure and scrutiny associated with listed companies, are more sensitive to the monitoring process; non-executives are expected to play the role of executive champion rather than corporate policeman.

Involvement in the setting of executive remuneration

Agency theory focuses on the relationship between shareholders and executives, and suggests that shareholders, as residual risk-takers, should represent the only interests that occupy executives (Jensen and Meckling, 1976; Fama, 1980; Fama and Jensen, 1983). Executives are presumed to be self interested, managing the presentation of information in order to influence compensation (Cannella and Monroe, 1997). The theory suggests that executives underperform without suitable corporate incentives which align them with shareholders (Grandori, 1996), and that equity ownership serves the dual purpose of aligning the interests of shareholders and management (Jensen and Meckling, 1976), and incentivising executives to take appropriate risks (Fields and Keys, 2003). Although agency concerns are recognised amongst respondents, this research provides strong support for both institutional and legitimacy theory; companies appear to be greatly influenced by mimetic isomorphic pressures and external visibility (DiMaggio and Powell, 1983; Scott, 1995; Suchman, 1995). Remuneration packages are structured not to enhance individual performance but to meet best practice (Bender, 2003b), heavily influenced by input from external consultants and criticism from institutional shareholders and the media (McNulty *et al.*, 2002; Certo *et al.*, 2003).

On unlisted boards non-executives have a lesser involvement in the setting of executive remuneration. Motivation is in many cases directly linked to long-term corporate success, and in some cases to real ownership, supporting elements of stewardship theory, stakeholder theory and shareholder alignment. Shared values, such as lack of egotism and single-minded self-interest, appear to be more common, and employees appear to be less dependent on short-term financial incentives (Davis *et al.*, 1997). Executive alignment benefits from the clarity and transparency of shareholder agendas. There is evidence, particularly in family companies, that executives are motivated by non-financial, intangible gains (Herzberg *et al.*, 1959; McClelland, 1961; Argyris, 1964; Herzberg, 1966; Donaldson, 1990; Donaldson and Davis, 1991; Muth and Donaldson, 1998), and in VC-backed companies executives are naturally aligned with shareholders to achieve their combined stated objectives over an agreed period of time.

The lack of external visibility from institutional shareholders, the regulators and the media allows unlisted companies much more freedom in the way that executive remuneration is structured, and reduces the need for formal independent committees. This research suggests that due to shareholder dominance, executive stewardship and equity alignment, non-executive directors can find themselves excluded from the remuneration debate, or at best with very little influence.

Involvement in appointing and removing executive directors

Agency theory suggests that the market for corporate control can curb the self-interested behaviour of senior executives; if executives are underperforming, and existing shareholders do not replace them in a timely fashion, external investors can purchase the firm and replace both the board and the management (Cannella and Monroe, 1997). Emphasis on the monitoring role encourages non-executive directors to overturn poor decisions, or replace underperforming executives as a result of such monitoring in a timely fashion (Brudney, 1985). Furthermore the theory identifies the executive labour market as an effective control mechanism on self-interested executives through the threat of dismissal and replacement; poor performance is a consistent predictor of executive turnover (Cannella and Monroe, 1997).

Due to the formal channels of communication within listed companies, and the increasing external attention on corporate governance and proper process, the process of appointing and removing directors is highly structured and transparent, making employee expectations easier to manage. The process of appointing and removing directors often involves a complex and lengthy negotiation; in many cases executives may have developed strategies which bond them to the company and make it difficult for the board to remove them, and in cases where the CEO power is high relative to the board, attempts at removal may not be successful (Cannella and Monroe, 1997). The process is highly visible to external constituencies, who are increasingly critical of rising divorce costs. Furthermore, price-sensitive information demands a unity of board process; non-executive directors consider board alignment as an essential part of the process.

On unlisted boards this research suggests that there is a more complex alignment between shareholders and executives, often inextricably linked by ownership of equity amongst executives and a blurring of board roles. Appointing and removing directors can illuminate strong personal and emotional opinions based on individual history and culture amongst incumbent shareholders and executives; unlisted companies can hire and fire without attracting the attention of external constituencies or the requirement for board sanction, and there is further evidence that dominant shareholders impose undue pressure and lessen non-executive activity.

Involvement in succession planning

For non-executive directors, the identification of a competent heir apparent not only smoothes routine CEO succession, but also provides insurance should anything unexpected happen to the incumbent CEO (Vancil, 1987; Lorsch and MacIver, 1989). External visibility, shareholder activism and regulation have influenced the way that listed companies approach succession planning, and there is now an obligation to discuss the process in a transparent and timely fashion. The process is complex; although there are often identifiable internal candidates, executive sensitivities are high, and few CEOs are prepared to relinquish power in a timely fashion (Cannella and Shen, 2001).

On unlisted boards non-executives have a lesser involvement in the process of succession planning. Companies are less influenced by isomorphic pressure and external visibility, and succession planning is often characterised by severe internal political manipulations and power struggles (Pfeffer, 1981), largely determined by the distribution of power among the parties involved (Boeker and Goodstein, 1993; Cannella and Lubatkin, 1993; Zajac and Westphal, 1996). External candidates may be more difficult to attract, and there are fewer internal candidates. Furthermore, shareholder dominance increases the sensitivities; in both family-owned and VC-backed companies, shareholders have a direct influence on the composition and succession of the senior management team, discouraging independent views.

Areas of great importance across listed and unlisted boards

Although non-executive involvement varies between sectors, there are significant areas of commonality between listed and unlisted boards. Non-executive directors consider risk analysis, subject to the vagaries of the market and the human condition, and the process of board induction equally important across listed and unlisted company boards.

Importance of risk analysis

On listed boards the process of risk analysis is a priority on the non-executive agenda, partly due to the visibility of corporate failure. Non-executive directors, conscious of the issues of accountability, are protective of their reputations as expert decision makers (Fama and Jensen, 1983), and are aware of the trust placed in them by investors who have little data on which to base a judgement on the quality of management and future performance (Certo *et al.*, 2001). Distance from operations is great, reliance on executive knowledge is high, and processes are formal and highly structured.

Although agency issues are lessened, and companies are likely to be less complex, non-executives on unlisted boards consider risk analysis a high priority. The task is facilitated by a familiarity of company operations; some directors have a substantial ownership, some have unlimited time to spend with the company and attend informal meetings with management and shareholders (Hill, 1995). Executives and shareholders rely heavily on non-executive identification of risk; unlike their listed counterparts shareholders they do not have widely diversified investment portfolios and are subject to wealth destruction in the event of failure (Cannella and Monroe, 1997). Furthermore, unlisted companies have less structured processes and financial disciplines in place, suffering from a liability of smallness (Finkle, 1998) and limited executive experience, making them more vulnerable to the unpredictable nature of risk and unstable conditions and more reliant on non-executive input.

There are no guarantees; respondents noted that corporate governance, whilst improving the processes and systems of analysis, does not replace the value of corporate quality, reliability and culture. The tangible cannot override the intangible; the thoroughness of structure and the frequency of debate cannot diminish nor replicate the board's dependence on individual integrity and the comfort of trust.

Importance of induction

The process of induction is recognised across sectors as an increasingly important requirement for non-executive directors. In many cases induction onto listed boards has become more formalised and thoughtful in order to maximise effectiveness and raise risk awareness.

On unlisted companies, many of which are smaller and less complex than listed companies, induction is considered no less important, although it is often non-executive led. Benefiting from informal channels of communication, non-executives are expected to have specific knowledge of company operations and sector risks in order to add value whilst avoiding executive interference.

Areas of lesser importance on unlisted boards

Respondents identified two roles of lesser importance on unlisted boards. The role of development, although viewed with scepticism on listed boards, is considered to be of no value to experienced non-executive directors serving on unlisted boards. Furthermore, the value of independence, both structural and philosophical, is diminished in the presence of dominant shareholders and, if contrary to shareholder views, can prove a barrier to effectiveness.

Importance of development

There are parts that corporate governance cannot reach; the Combined Code (FRC, 2003) has not yet influenced non-executive attitudes to boardroom development, often inhibited by language, generation and custom. Directors, dismissive of formal development and unclear about its benefits, reluctantly admit the value gained by informal external debates hosted by firms of accountants and headhunters.

On unlisted boards, however, the response is more defined; without the pressure of regulation and public scrutiny, board development is considered an unnecessary and costly exercise. The cross fertilisation of ideas and experiences across sectors, the alignment between executives and shareholders, and the conscious adoption of PLC policies and practices are considered priority contributions on unlisted boards, who benefit directly from those directors already serving across sectors.

Importance of independent judgement

The principle of independent judgement is perhaps the most complex for non-executive directors to evaluate across sectors. In theory independent judgement is vital for effective contribution (McNulty *et al.*, 2002), described picturesquely as a lighthouse on a dark and stormy night (Daily and Dalton, 2003). There appears to be an assumption within UK regulation that structural and psychological independence is linked, legitimising non-executive individual power and authority within the boardroom. However, this research indicates that non-executive directors view independence as a state of mind (Gay, 2001), the effectiveness of which is either encouraged or inhibited by personality and board dynamics rather than tangible and dependent associations.

In many ways independence goes to the heart of the non-executive comparison between listed and unlisted company boards. This research suggests that structural independence has little obvious meaning and value on an unlisted board; there is no institutional requirement to appoint non-executive directors, to limit their tenure or to establish their independence. Unlike their listed counterparts, dominant shareholders do not view their boardrooms as dark and stormy, nor do they necessarily benefit from the lighthouse of independence. Powerful shareholders, such as established and prestigious families, can have a devastating effect on the psychology of the weak non-executive director, and the role demands an intuitive and sensitive understanding of the cyclical, structural, cultural and procedural influences at work. In VC-backed companies independence is even less welcome; boards often have investor representatives on the board who do not value the debate and challenge introduced by independent voices, and who consider block equity ownership a more appropriate governance mechanism (Wright and Robbie, 1998). This research indicates that non-executives on unlisted boards are expected to fulfil many roles, but independence is not necessarily one of them.

Discussion and conclusion

This paper presents a snapshot of the research findings, and can only give an initial indication of the research contribution. There is evidence that the non-executive director, although concerned primarily with the role of protection, has a polarised view of the world on a listed and an unlisted company board, which is influenced by levels of shareholder power and presence, lifecycle, visibility, isomorphic pressure, information asymmetry and the impact of corporate governance and regulation. Supportive of the literature this research suggests that on listed company boards non-executive directors are concerned primarily with institutional, agency and management hegemony issues, i.e. they are protecting the long-term interests of fragmented and anonymous shareholders from the short-term ambitions of knowledgeable and self-interested executives (Mace, 1971; Fama and Jensen, 1983).

On unlisted boards the role is very different; non-executive directors have a breadth and depth of contribution which goes beyond the Combined Code Guidelines (FRC, 2003). The role, facilitated by close and informed board relationships, and familiarity with company operations, is unaffected by external visibility, isomorphic pressure and price-sensitive information, and more involved with the strategic and financial processes, the alignment of shareholders, and the cross-fertilisation of experiences than on a listed board. Non-executives on unlisted boards are less concerned with agency and management hegemony issues due to the close alignment and transparent agendas of executives and shareholders, but are preoccupied with the issues of shareholder dominance, which influence the management and monitoring of executives and the protection of minority shareholders. This begs the question of whether, even on listed boards, non-executives should focus only on the interests of shareholders as suggested by recent guidelines, or whether their role would be more effective and fulfilling if concerned with the wider issues associated with the alignment of shareholders and executives over the longer term.

The role of the non-executive director serving across listed and unlisted boards incorporates the adoption of practices across sectors. On listed boards non-executives encourage closer and more knowledgeable relationships with executives in order to assist the strategic and financial processes, and the flexibility of board contribution. On unlisted boards non-executives, benefiting from PLC disciplines and experiences, encourage clarity of roles and expectations, the disciplines of procedure in the face of public scrutiny, and the development of people management and monitoring in the presence of dominant shareholders. The polarisation of roles diminishes in the face of cross-sector experience, allowing non-executives the opportunity to contribute effectively and appropriately, and to measure and evaluate their contribution in the context of each individual boardroom. This research suggests that it is not the sector that encourages or inhibits the non-executive role, but that it is an individual's sensitivity to the cyclical, structural, cultural and procedural dynamics inside and outside the boardroom which ultimately dictates whether original authorship, or sensitive translation, will maximise effectiveness.

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