Going Public

How to prepare your board for IPO

ODGERS BERNDTSON
Search Intelligence

Executive Summary

Is the market for initial public offerings back?

After a long, dormant period for new issues caused by the financial crisis and recession, the pipeline of potential flotations is reportedly strong.

But the markets remain volatile, and investor demand for high-priced or risky floats is weak.

In this environment, it is more essential than ever that pre-IPO companies are led by a strong and effective board of directors.

A high-calibre chairman and board will help management teams make the cultural transition from private to public hands. It can bring its knowledge to bear on risk management, internal controls, investor and media relations, and corporate governance.

It can ensure that the IPO process does not detract from the successful running of the business, and give investors the confidence to back the float.

This paper looks at the questions that companies preparing for IPO should be asking about the composition of their board.

- How many non-executive directors should be appointed, and from what backgrounds?
- What skills and experience are needed in a chairman?
- Which provisions of the UK Governance Code must be applied in advance, and which may be incorporated over time?
- What differences of approach are required if the listing is planned for Aim versus the Main Market?

Odgers Berndtson has extensive experience in advising pre-IPO companies on critical board appointments. We have drawn on interviews with directors from companies that have recently floated or are planning to do so, as well as from City advisers and private equity professionals.

The result is a 'how to' guide on getting your board right, and so maximising the chances of a successful flotation.

Planning Ahead

A company contemplating a future flotation should begin the process of building the right board as far in advance as possible.

The three to six months immediately before an IPO will be dominated by document preparation and investor roadshows, making it a poor time to appoint, induct and develop a board. New non-executive directors should be brought on board at least six months before; a year in advance is better. This approach also allows time for unsatisfactory appointments to be weeded out.

Patrick Dunne, former Group Communications Director at private equity group 3i, says: "You need time for the board to gel. It's not only about picking the right people, it's about building the team."

Peter Williams, Senior Independent Director of ASOS and appointed a non-executive director of Cineworld a year in advance of its £240m debut on the London Stock Exchange, says: "The non-executive directors need to form a relationship with the executive team well in advance of the IPO, because you want to present the market with a unified, cohesive board."

David Maloney, who served as a non-executive director on the boards of five companies undergoing flotation, says: "As a non-executive director, you need to join before the paperwork starts. You need to be in at the beginning when the key decisions are made."

New directors need time to immerse themselves in the company, adds a veteran non-executive director of several IPOs. "Be part of the business, build your networks in the organisation so you are familiar with the culture of the company and not just the information brought to the board," he says.

Few privately-held companies can realistically have a Plc-ready board in place a year in advance of a potential IPO; nor does the market expect this. "Investors are looking for the nucleus of a strong board, but they don't expect it to be fully formed," says Phil Hodkinson, a non-executive director at BT and also a non-executive director of Resolution Ltd., the insurance group, at the time of its flotation on the London Stock Exchange.

Companies should adopt a dynamic approach to appointments, building the board as the deadline approaches. The first critical appointments are plainly those of Chairman and, in the event that the chairman is not independent, the senior independent director.

Next, City audiences will expect credible non-executives to be appointed to chair the audit and remuneration committees. Three non-executive directors is probably the minimum number of appointments to be made well in advance of the flotation.

Thereafter, depending on the size of the company being floated, the company may wish to take a more considered approach to further recruitment. This allows time for the core of the board to develop its knowledge and working style, and for remaining gaps in skills and experience to be identified. In the words of one Nominated Adviser: "The market doesn't want to see the whole board replaced ahead of the IPO – that betrays a lack of continuity."

There may be value in finalising board appointments closer to the IPO, or even after it. "As the IPO becomes more certain, it becomes easier to attract good non-executives," says Hodkinson.

As a non-executive director, you need to join before the paperwork starts. You need to be in at the beginning when the key decisions are made

Life as a listed company can be very alien to an executive team that is not used to dealing with it

Summary: Plan as far ahead of the IPO as possible, but maintain a flexible approach, introducing new directors to the board as appropriate in advance of the IPO, and after it, to ensure the best possible people are recruited.

The focus of the NED role

A principal task of newly appointed non-executive directors ahead of an IPO is to ensure that the company is properly equipped for life as a public company. Necessary changes may include putting in the essential corporate governance 'plumbing', such as board committee terms of reference, internal controls and accounting policies.

One experienced non-executive director says: "You can't go to the market until you have all the disciplines in place."

Peter Williams says: "You need your non-executive directors to be involved in setting up the terms of reference for the various committees, and ensuring that the remuneration is right and won't raise eyebrows."

Phil Hodkinson adds: "Sort out the governance and accounting structures and policies first. You won't have the resources or management capacity to do that and float the business at the same time."

Cultural change within an organisation may also be necessary ahead of an IPO, as managers adjust to the scrutiny that comes with a public quotation. Williams says: "Life as a listed company can be very alien to an executive team that is not used to dealing with it."

The legal and regulatory demands, the volume of reporting, and the sheer amount of time spent on investor relations can be surprising and frustrating for managers who are accustomed simply to running the business.

It is the board's job to ensure that the right governance structures are in place and that management buys into the need to make them effective. "It's not enough just to get the documents written," says Hodkinson. "The board must have the experience to recognise whether the audit committee terms of reference or risk management policies are fit for purpose, and sufficient influence to ensure they are applied."

The appointment of an experienced company secretary and/or general counsel may be as critical as any other board appointment. "It's imperative you have someone who's on top of all the regulatory filings, governance expectations, reporting deadlines and so on, because there's a world of difference between running a privately-held company versus a quoted one," says Williams.

The governance plumbing should be appropriate to the company's size and complexity. Investors will expect companies listed on Aim to take advantage of this market's less onerous listing rules. "They want companies to be more fleet of foot, nimble, and to pay less for the trappings of being a public company," says Hodkinson.

Other aspects of the non-executive's role in the run up to the listing date include ensuring that the IPO doesn't distract management too much from doing the day job. Williams says: "The management team will have spent all their time running the business; suddenly they're spending 95% of their time getting the float away. It's the board's job to help them cope with the extra responsibilities while also ensuring that the company continues to be well run."

David Maloney adds that a critical element of the board's job is seeing that the company gets sound counsel and value for money from its City advisers. "It's a minder role," he says.

Summary: Focus on introducing public company governance structures as soon as possible, and certainly well ahead of the demanding document preparation phase of the IPO.

Building the right relationship in the boardroom

The non-executive director's role is a subtle one, involving both supporting and challenging the executive team. Establishing the right mix of collegiality and oversight is especially important in a pre-IPO company where the business is facing a transformational change.

The challenge of building a cohesive board is complicated by the fact that the personal interests and motivations of the people round the board table can be markedly different. The executive team may have a strong motivation to get the deal done, perhaps to realise considerable wealth. The non-executive directors should be sensitive to the risks of making exaggerated or misleading representations to the market. "That is where the quality of the chairman comes in," says Phil Hodkinson.

Dunne adds: "Balancing the passion and commitment that founders bring, with the need for objectivity and an ability to recognise when fundamental changes have to be made, is a particularly difficult challenge in pre-IPO companies." Both executive and non-executive directors must be open about the fact that there will be disagreements ahead and seek to build the right relationship that will ensure those disagreements are not fatal.

One non-executive director with experience of several IPOs says that management teams realise they need a board appropriate to Plc status, but often don't always recognise that this board wields ultimate decision-making authority. "They want a mentor, but somehow expect that decisions will remain with them. They've been successful in the past – why should they be challenged now? It is important that the executives appreciate that the board adds value, and that it's not just there as a check and balance. Holding proper board meetings is a discipline that founders often need to learn. You can't introduce that on the day after the IPO," he says.

Summary: Both executive and non-executive directors need to invest time in developing the relationship so that it can withstand the test of tough, unpopular decisions. Prospective non-executive directors need to carry out their due diligence to ensure they are joining a board where they can exercise influence.

Selecting the right NEDs

As on any board, the right balance of skills and experience is critical in a pre-IPO situation. While helpful, it is not essential to have a director who has been through an IPO before. "That is what the advisers are there for," says one non-executive director.

Nor is it necessary to have non-executive directors with sector experience, though this depends on the sector in question. Highly technical businesses probably do require at least one non-executive who is familiar with the industry. In more easily understood sectors, general business

The board must have the experience to recognise whether the audit committee terms of reference or risk management policies are fit for purpose, and sufficient influence to ensure they are applied

A director accustomed to FTSE 100 status may not necessarily have the right mindset to understand the specific challenges of a high-growth entrepreneurial company, or may chafe at the fact that company secretarial resources are scarce

experience and commercial nous are arguably more important.

Patrick Dunne says: "Situational experience is most important. In other words, does the non-executive director candidate have a relevant track record in M&A, internationalisation, or succession planning for senior roles? Relevant sector experience matters but is secondary."

One broker and Nominated Adviser said: "If you're appointing two non-executive directors, one person should have experience of the City, whether as a lawyer, accountant or corporate financier, while the second should probably have sector experience. The right mix and balance are vital."

In the wake of the financial crisis, appointing a City 'heavyweight' may have an even greater appeal as pre-IPO companies seek to bolster the confidence of wary investors. But boards should be sure that they are not appointing directors solely on their ability to lend gravitas and 'a name' to the prospectus. As with any appointment, boards must be clear that non-executive director candidates bring skills and experience that are aligned to the objectives of the business.

A second Nomad said: "If they have a City background, they could contribute to roadshow presentations or help shape the marketing message, while a non-executive with industry experience should put relevant contacts and skills to good use. In my experience, the non-executives who are less successful are those who focus solely on the policeman/watchdog role and forget they are there to add value."

A final consideration is also to ensure that past board experience is relevant and appropriate. A director accustomed to FTSE 100 status may not necessarily have the right mindset to understand the specific challenges of a high-growth entrepreneurial company, or may chafe at the fact that company secretarial resources are scarce.

Summary: Appoint directors with an appropriate mix and balance of sectoral and situational experience, so that the board's make-up reflects the objectives of the company. Ensure that the experience of non-executive director appointees is relevant to the company's size and ambition.

Look beyond the IPO

The demands of the flotation process can be sufficiently intense to distract boards from focusing on life after the IPO, but the first months and years after listing are critical to establishing sound investor relations. "You don't want the child struggling in its early years," says Peter Williams.

The board also needs to ensure the public company culture, carefully cultivated ahead of the IPO, survives the first day of trading. David Maloney says: "Managers understand that the IPO process is a significant amount of work – it's after the float that the corporate governance demands can be very frustrating."

One non-executive director adds: "The weight of obligations is often not fully realised. The management team can sometimes think that they will carry along as they always have."

This underlines the importance of ensuring all the governance machinery, especially the financial reporting process, is in place and working effectively ahead of the IPO. A blinkered approach focused solely on getting the float away is a sure recipe for later trouble. In the words of one adviser:

"Investor relations will be a new skill that management and the company will have to work hard to develop."

Long-term commitment can be demonstrated by newly appointed non-executive directors putting their hands in their pockets to buy some stock in the company. "They should be seen to be backing the issue," says Williams.

Summary: Don't let the IPO process distract the board from paying close attention to medium and long-term strategy so that the company has the best chance to flourish as a listed business. Ensure that the good governance disciplines put in place for the IPO are maintained and updated where necessary.

Conclusion

In difficult markets, investors want reassurance that companies coming to market are led by high-calibre boards that know and understand the business. They look for boards that offer continuity as well as competence

Preparing a company for an IPO is never an easy task. But in today's markets, characterised by uncertainty, volatility and investor skittishness, the challenge expands exponentially.

Even the best-planned IPO can fall victim to unforeseen circumstances. In early 2010, several prominent flotations were cancelled after a strong rally in share prices swiftly went into reverse.

Companies can do little to prevent their IPO being torpedoed by prevailing market conditions, but they do exercise control over the make-up of the board of directors. This is an increasingly critical factor in ensuring that an IPO goes to plan.

In difficult markets, investors want reassurance that companies coming to market are led by high-calibre boards that know and understand the business. They look for boards that offer continuity as well as competence.

In such circumstances, pre-float companies gain a head start if they can demonstrate that their board has been properly inducted, and that the non-executive directors have toured operations, met the management teams below board level, and gelled as a team. This requires foresight and planning.

It is tempting for companies planning an IPO to allow their lawyers, accountants and City advisers take the lead. But well before those consultations become advanced, the company should focus on preparing and strengthening its board. Such an approach not only maximises the chance of the floation succeeding, but gives the company the best possible chance of flourishing as a quoted business.

As Patrick Dunne says: "Set the board up in the right way for the future. Getting it wrong initially can damage the company for a long time to come."

About Odgers Berndtson

Odgers Berndtson is one of the leading international executive search firms and the largest in the UK. Our reputation for excellence and integrity has been established over 40 years. We act as trusted advisors to clients who need help recruiting for important positions.

Odgers Berndtson's Board Practice is responsible for some of the most important recent Chairman and Non-Executive Director appointments as well as for executive board roles.

As part of a truly global firm, the Board Practice spans all major markets. We work with a wide range of FTSE and AIM-listed companies, international groups, private equity-backed businesses, family-owned organisations, and small and medium sized enterprises.

We have a thorough understanding of board and committee structures, and board dynamics. Our team includes experienced directors of publicly quoted and privately held companies. In short, we know how boards work.

Odgers Berndtson has been an influential voice in the corporate governance debate. We understand how the principles of good governance, applied practically and not by rote, can help create strong, effective boards that add real value to an organisation.

Our wide experience and deep knowledge is brought to bear on every board appointment we undertake.

Our People

Virginia Bottomley

Virginia chairs the Odgers Berndtson Board Practice. The Board Practice conducts searches for chairs, chief executives and non-executive directors for plcs and private companies.
virginia.bottomley@odgersberndtson.com

Kit Bingham

Kit is Partner and Head of the Chair & Non-Executive Director Practice. He joined after a career in financial journalism and financial public relations. He is a member of the Business Committee of Policy Exchange, the think-tank.
kit.bingham@odgersberndtson.com

Contact Details

Tel: 020 7529 1111

Global Offices

UK Offices

England

London
20 Cannon Street
London EC4M 6XD
+44 (0) 20 7529 1111

Birmingham
9 Brindleyplace
Birmingham B1 2HS
+44 (0) 121 654 5900

Manchester
Suite 16E
Manchester
International Office
Centre
Styal Road
Manchester M22 5WB
+44 (0) 161 498 3400

Leeds
10 South Parade
Leeds LS1 5QS
+44 (0) 113 386 8500

Scotland

Glasgow
Stock Exchange Court
77 Nelson Mandela Place
Glasgow G2 1QT
+44 (0) 141 225 6320

Aberdeen
7 Albert Street
Aberdeen AB25 1XX
+44 (0) 1224 218 999

Wales

Cardiff
13 Cathedral Road
Cardiff CF11 9HA
+44 2920 783 050

ODGERS BERNDTSON
Search Intelligence