


Company *Matters*

January 2020

Board diversity in AIM and FTSE Small Cap companies



Welcome to this first report on the important subject of 'diversity for smaller companies'.

Why did we undertake this piece of research? Easy, there is a lot of research measuring the FTSE 350 and whilst those companies account for a big slice of the economy not all of them are UK based and many are large global corporates. So is there merit in looking a bit wider and seeing what's happening below the FTSE 350? We think so. In our sample the companies are almost all UK and in the FTSE small cap or listed on AIM. An interesting and diverse group of businesses, but are they paying attention to what is happening from a societal perspective where the public want more transparency and to understand and trust business once again. Perhaps we can start to make greater and faster change with some of the smaller companies as opposed to expecting everything to come from some of the global monoliths of the FTSE 350 which can feel removed and distant. Can trust be built from smaller sound UK businesses 'doing the right things' and behaving as 'good corporate citizens'? So let's start by shining a light on some and see what is happening. Diversity and the metrics we have chosen are a starting point for a conversation and a foundation on which to build in the future, it is by no means perfect but it is a start.

Thank you to the entire Company Matters tribe who contributed to the collation of the data. A bigger thank you to Caroline Emmet and Paul Johnston aka the Techie Gurus who led the research. Welcome and thank you to Dr Scarlett Brown who brought together this report and provided external validation for the work.

We did it because we care about doing the right thing and we hope it leads to meaningful conversations which lead to meaningful actions in this area.

Yours



Tracey Brady

Overview

Board diversity has been on the agenda in the UK for the best part of a decade.

With an increasing focus on gender diversity, a target was set in 2011 for FTSE 100 companies to have a 25 per cent female board. This was met in 2015, after which the voluntary target was extended. The Hampton-Alexander review¹ raised the bar to 33 per cent for FTSE 350 companies which should be met in 2020.

Of course, diversity isn't just about gender. In 2017, Sir John Parker illuminated the issue of ethnic diversity, suggesting the FTSE 100 should have one director 'of colour'² on their board by 2021 and the FTSE 250 by 2024. Although meeting this target seems less likely, ethnic diversity on boards is slowly increasing.

The idea of board diversity has gone from radical to widely accepted as what makes boards work well. Companies have seen growing pressure to up their game on values, purpose, stakeholder engagement and culture. Major investors are now more likely to vote against re-election of the nomination committee chair if demonstrable progress isn't made and if the minimum thresholds of female representation aren't met. Boards are not asking 'why' anymore, they're asking 'how?'

In the background, less attention has been on board diversity in companies below the FTSE 350, despite encouragement to consider and report on their diversity. This includes reporting on gender pay gap,

UK corporate governance code, QCA code, board diversity policy disclosure requirements and the Hampton Alexander Review. The results within shed a light on diversity in these companies.

We analysed the boards of 100 largest companies of the FTSE Small Cap index (FTSE SMC 100) and in the AIM 50 index by looking at their annual reports and appointments². We reviewed their board diversity and how they report on their approach.

We've found that board diversity in these indexes is increasing but it remains low, particularly in the AIM UK 50. In these companies, 15 per cent of directors are women and 36 per cent have all-male boards. These figures are barely higher than the FTSE 100 in 2011.

We've seen more encouraging results in the top 100 companies of the FTSE Small Cap index which, at the time of writing, has a gender balance of 28 per cent women (better than the FTSE 250). This is fairly recent as 44 per cent of new appointments in this index over the last 18 months were women, which is a higher rate than the FTSE 350.

We can only hope this is the direction of travel. Women hold four to five per cent of executive roles in these companies and this is notoriously slow to change in all markets. The majority of these women are in CFO or DF roles, suggesting they have an 'easier' route for women to executive roles in the boardroom – even though women are no

1 Hampton-Alexander Review, FTSE Women Leaders (November 2016 report and subsequent updates published annually).

2 Further detail can be found in our methodology section on page 15. .

more likely to have financial experience than men. This is similar to the FTSE 350 where 60 per cent of female executive directors are CFOs or FDs.³

Ethnic diversity is low on these company boards too, showing very little change. More than 95 per cent of directors are white and over 80 per cent of boards are all-white. There are some exceptions where a board has more than one non-white director, but these are rare and typically non-UK incorporated or domiciled.

We've found that these companies have greater age diversity on their boards, particularly in male directors who range from 40 to 80+. This is partly because male non-executive directors have longer tenures and are more likely to be in executive roles, which tend to be younger. The average age of directors is slightly lower than the FTSE 350.

Another big change in the last few years has been higher expectations for companies to report accurately and transparently on:

- Their board diversity policies
- How they're meeting targets (if at all)
- How their nomination committees account for diversity in appointments

This reporting should give investors and stakeholders better insight into their board processes, but a review by the FRC found that this is a fairly weak area of reporting in the FTSE 350.

We also found patchy reporting in our sample. In the FTSE SMC 100, more than half have basic or boilerplate reporting. Nearly one in six companies either state that they don't regard diversity as part of their appointments (ie an 'anti-diversity' policy), or fail to meet the code's requirements by not mentioning diversity at all. Figures are even worse in the AIM 50 UK, where 42 per cent have no mention or policy on diversity.

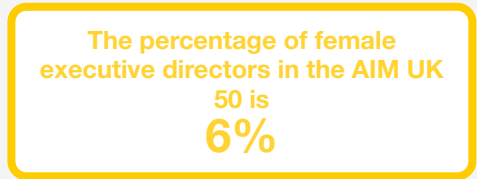
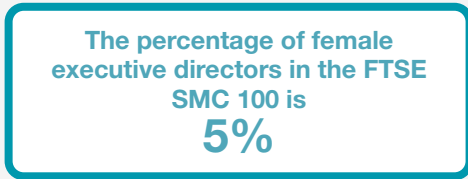
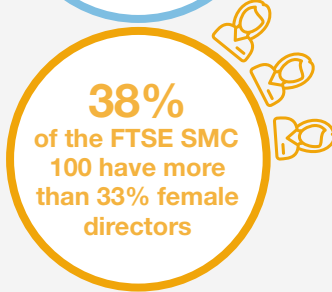
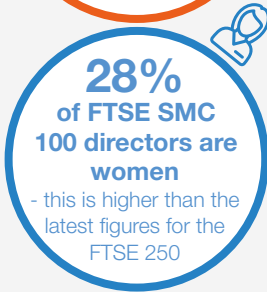
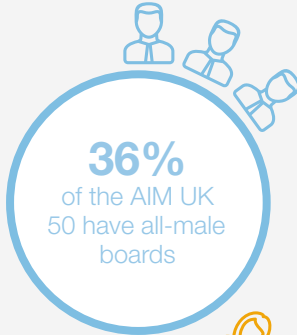
Companies often have inconsistent statements about board diversity spread across three or more sections of their annual report, making it difficult to identify their position on diversity or how they demonstrate accountability for change.

There are still reasons to be optimistic. In the FTSE SMC 100, companies are affected by the scrutiny placed on the FTSE 350. Many are making their way towards 33 per cent women on boards at a similar rate. There are also a handful of companies taking their reporting seriously, giving investors and stakeholders good visibility into their policies and accountability.

But there's still a long way to go. A review of the AIM market's reporting shows there are many companies making no attempt to engage with the need to diversify their boards or senior management. This is crucial, because companies in this index are a major talent pipeline for FTSE 250 EDs and NEDs.

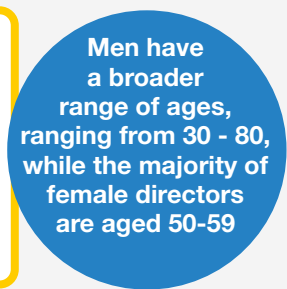
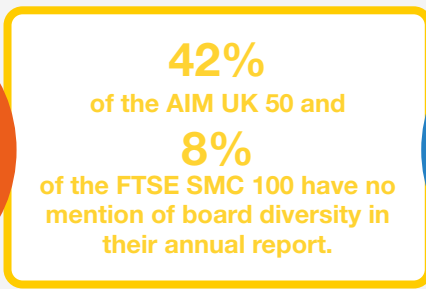
³ Cranfield University Review of Women on Boards, 2019.

Highlights



Ethnicity

on boards is lagging across the AIM and FTSE SMC 100 companies. 96% of directors on AIM UK 50 and FTSE SMC 100 companies are white, while 80% and 81% of these boards are all-white, compared with just 50% of the FTSE 100.



Board diversity

Gender

Overall, gender diversity on the boards of the AIM UK 50 companies is only slightly higher than the FTSE 350 was a decade ago, with 15% women directors (of a total of 329 directors). Most concerningly, over a third (36%) still have all-male boards. Since the annual reports were published, 43% of new directors are women - an encouraging percentage, although this is only nine women.

The proportion of women in executive roles is also low: women make up just 4% of executive directors and only one of these is a CEO. This is actually in line with the FTSE 350 now, and the executive director pipeline is notoriously slow. There are two women in Chair roles and another three female Senior Independent Directors (SIDs). One of the biggest challenges to progress is the 'One and Done' mentality - where boards appoint a woman to meet their diversity requirement but show little appetite for a second. It is encouraging to see companies avoiding this - Of the companies that have women directors, nearly half (15) have more than one female director, and eight companies (16%) have already met a target of 33% female board representation.

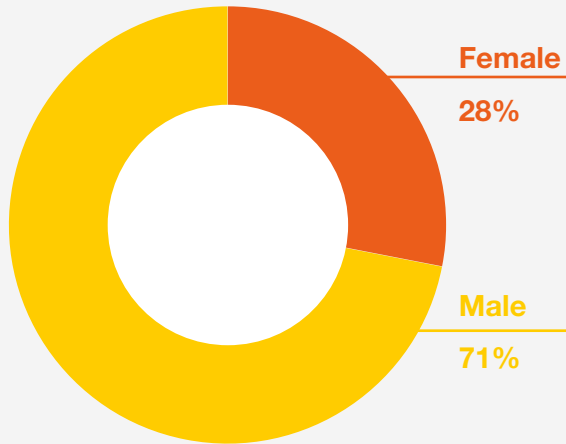
Gender diversity of the FTSE SMC 100 is higher than in the AIM UK 50 and is also, perhaps surprisingly, higher than the FTSE 250. Of the 607 directors in the FTSE SMC 100, 28% are female, taking into account appointments made since the last annual report, of which 44% were female. This is a notable shift and suggests that the tide may be turning on companies that have traditionally had very limited gender diversity, and are beginning to recognise the benefits of further diversity at Board and senior management levels.

There are six female executive directors in the FTSE SMC 100, representing 5% of all executive roles. Of these six, all but one are in CFO roles, suggesting CFO routes may be easier for women to reach executive board level than CEO. Five companies have a female chair and 19 have a female in the Senior Independent Director (SID) role - this represents a quarter of all SIDs in the FTSE SMC 100⁴. Since the annual reports have been published this has changed slightly: another two female executive directors have been appointed, including the only female CEO in the FTSE SMC 100.

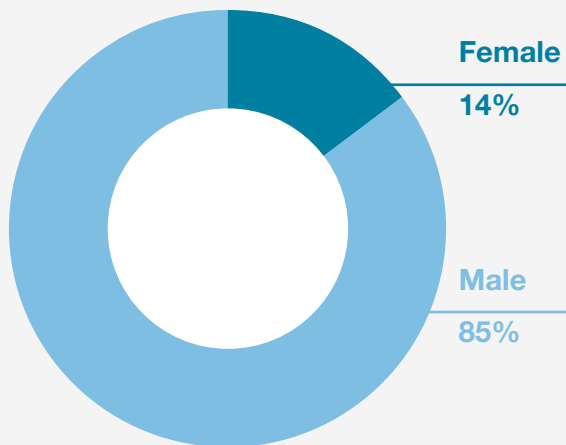
	FTSE SMC 100	AIM UK 50
Female execs	6	7
Female CFOs	5	3
Female CEOs	1	2
Female Chairs	5	2
Female SIDs	19	3

⁴ 26 companies do not have a SID listed.

Gender diversity of FTSE Small Cap 100
(including appointments since
annual report publication)



Gender of AIM UK 50 directors

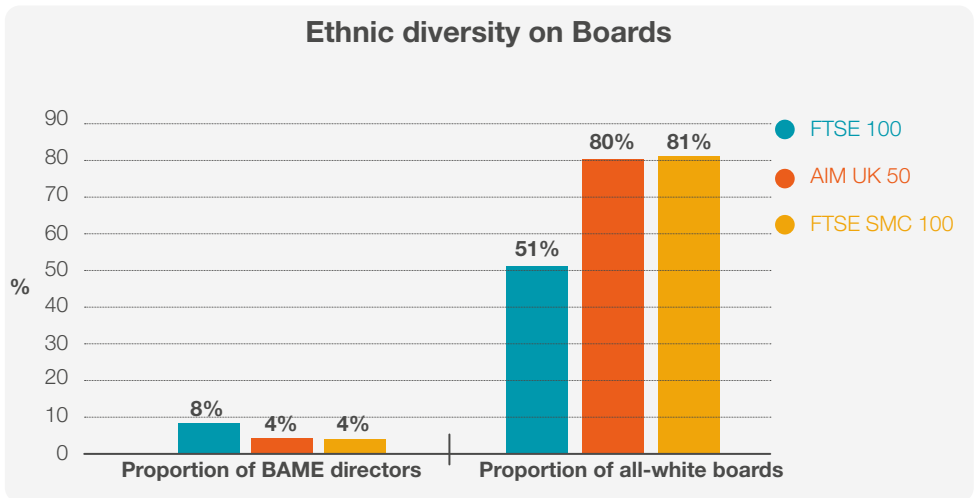


Ethnicity

The Parker Review⁵ drew attention to the lack of directors of colour on FTSE 350 boards, setting a target for boards to have ‘One by ‘21’, ie one director of colour on every board by 2021, and for the FTSE 250 to have one by 2024. Their review found, in 2017, that only 8% of the director population of the FTSE 100 are people of colour, a total of 85 people across 49 companies, with 51 all-white boards.

Our data shows that ethnic diversity is worse in the AIM UK 50 and FTSE SMC 100. In the AIM UK 50, at least 96% of Directors are white and 80% (40 out of 50) of companies have all-white Boards. Of the non-white directors, only one is female.

The percentages are similar in the FTSE SMC 100; 4% of directors are from Black, Asian or minority ethnic backgrounds and 81% of these 100 companies have all-white boards. Nine out of the 27 non-white directors (25%) are women.



Age

In the last decade the average age of directors in the FTSE 150 has risen by 2.1 years, and now sits at 60⁶. This is surprising given that board gender diversity has increased during that time, and that women directors tend to be younger. Directors in the AIM UK 50 and FTSE SMC 100 are younger than their FTSE 150 counterparts, with the average age at 57 and 59 respectively. As we would expect, NEDs and Chairs are consistently older than execs; the average age of non-executive directors is 59.7 in the AIM UK 50 and 60.2 in the FTSE SMC 100, and the average age of executive directors is 53. This is slightly below the average for FTSE 150 (54.3).

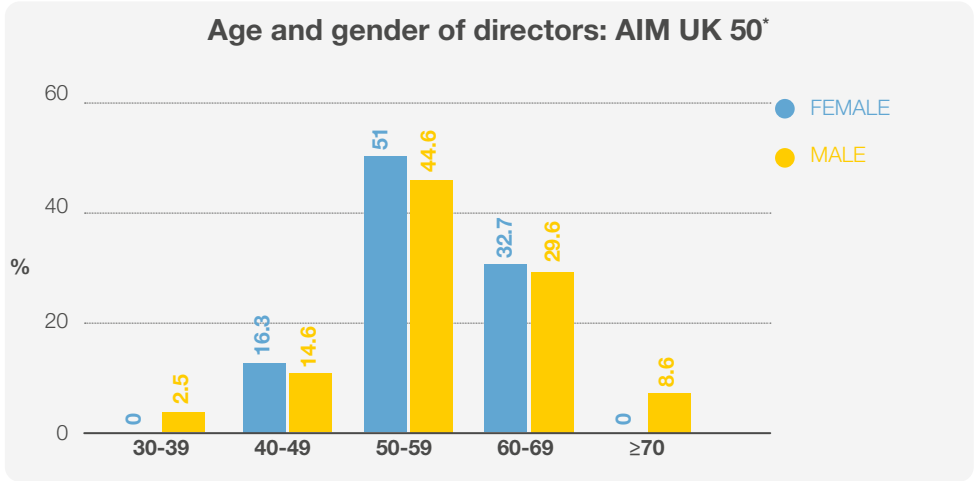
As in the FTSE 350, we find that the AIM and FTSE SMC 100 female directors are

⁵ A Report into the Ethnic Diversity of UK Boards. Final Report, The Parker Review Committee, 12 October 2017.

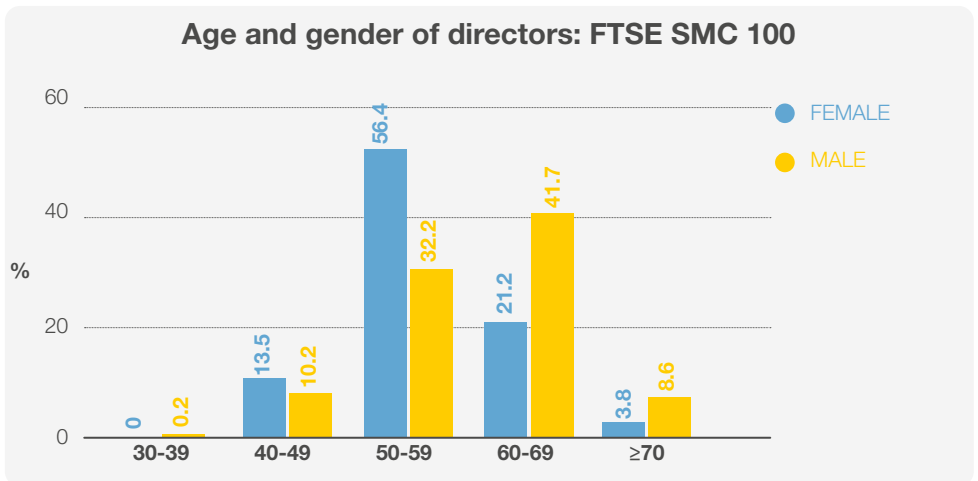
⁶ 2019 UK Spencer Stuart Board Index.

slightly younger than their male counterparts. In the AIM UK 50 the average age is 56 for women and 57 for men, in the FTSE SMC 100 it is 56 for women and 60 for men.

We see some interesting differences when we look at the range of ages for men and women. In the AIM UK 50 the range is much wider for men directors. The only directors under 40 are male (all executive roles), there are 24 over 70 and one director over 80: all are white and male.



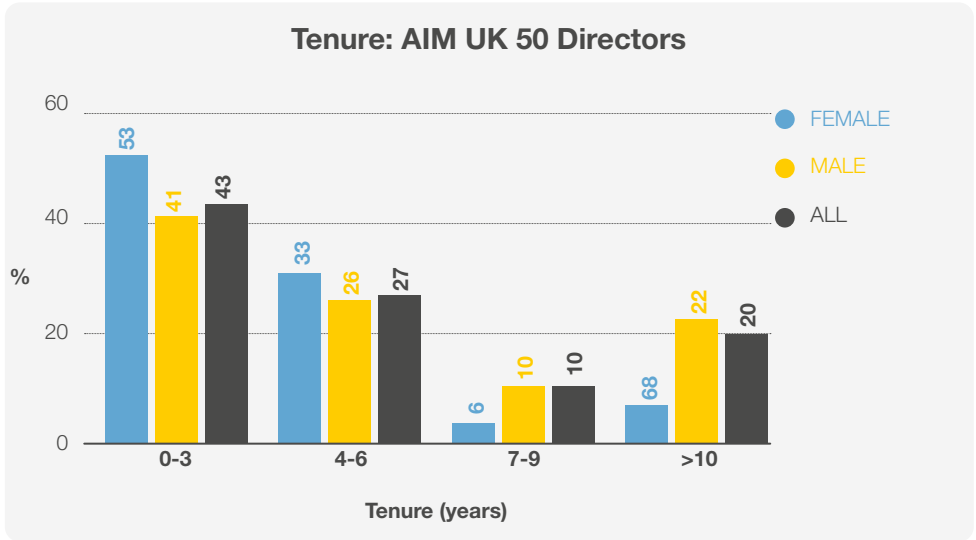
We observe similar findings in the FTSE SMC 100. The youngest and oldest directors are both men (30 and 80, respectively) while a large majority (56%) of women directors are in their 50s, compared with just under a third of male directors. This highlights two key findings - first it represents that executive directors are much more likely to be men than women, and that older NEDs with longer tenures with the company are much more commonly men.



* Unable to obtain information on the age of the directors of three companies.

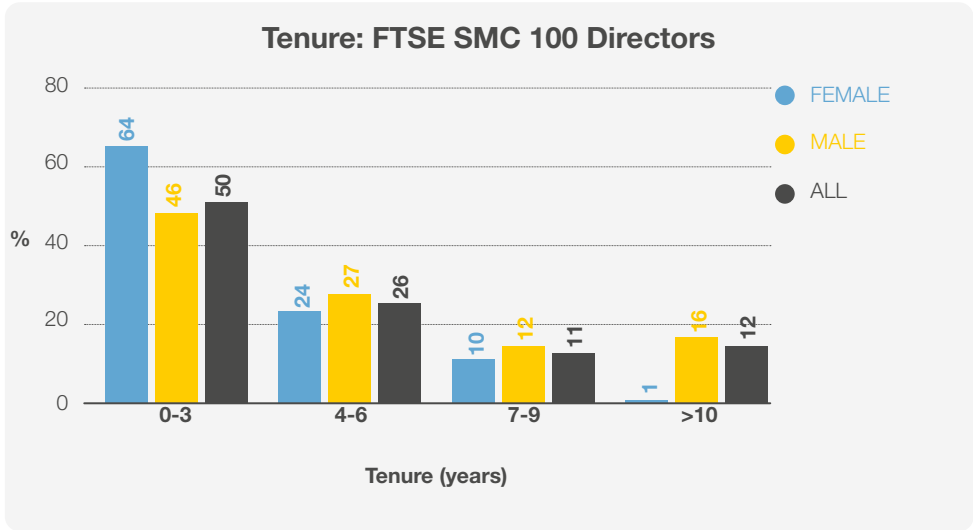
Tenure

Tenure of directors in the AIM UK 50 tends to be longer than in the FTSE 350 and the FTSE SMC 100, in large part because a number of directors for AIM companies are founder directors or are closely associated with the company more fundamentally⁷. Across the AIM UK 50, 3% directors have been in place for more than 20 years, and 17% for more than ten years. Generally women have shorter tenures: 53% of women directors have a tenure of less than 3 years compared with 41% of men, and this gives us a clear picture of how recent the focus on diversity is to AIM company boards.



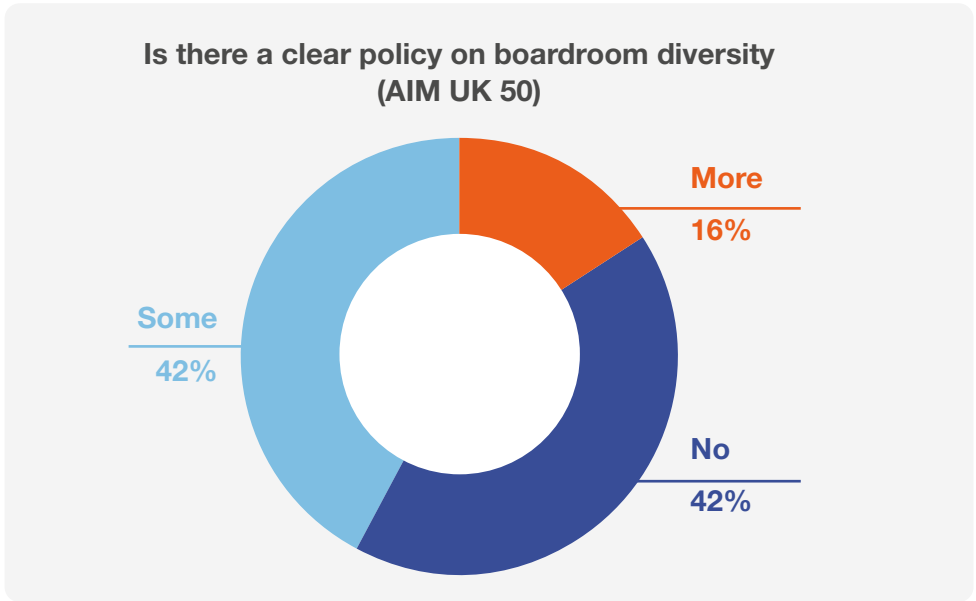
⁷ It should be noted that the data in annual report often does not capture the full tenure of long standing directors of companies that have been involved in restructurings or takeovers, and the numbers may therefore be much longer in some cases.

While overall tenure is shorter in the FTSE SMC 100 companies than in the AIM UK 50 companies - an average of 4.6 years compared to 6 in AIM. We see the same trend around gender; women directors have shorter tenures than their male counterparts. Thirty-two percent of male directors in the FTSE SMC 100 have been in place for more than six years, compared with only 14% of female directors, and of the 65 directors who have been in place for more than a decade, just four are women.



Reporting on Diversity

How a company reports on diversity - both at board and senior management level - can give us a valuable insight into how seriously they are taking it; whether they have a clear Board Diversity policy, and if they consider diversity to be important in appointments and succession planning. For those companies following the UKCGC this is expected as part of their annual reporting, alongside statutory reporting on the composition of the board, senior management and employees as a whole, mandatory for quoted companies (i.e. not AIM), and their gender pay gap which is mandated for all companies over 250 employees. In both cases, the reporting requirement should be driving discussion at board level.



Overall, reporting on diversity in the AIM UK 50 is less informative, both in comparison to the FTSE 350 and the FTSE SMC 100. 42% of the AIM UK 50 have no mention of board diversity in their annual report. Another 42% include a simple or boiler-plate response - a statement of commitment to diversity but with no specific details. Only eight companies have reporting that gives additional detail⁸ with only 9 companies explicitly stating they have a diversity policy. Just two set any measurable objectives for board gender diversity, while 18% mention gender as part of their director succession planning. 22% discuss initiatives they have in place for increasing gender diversity at their senior management level.

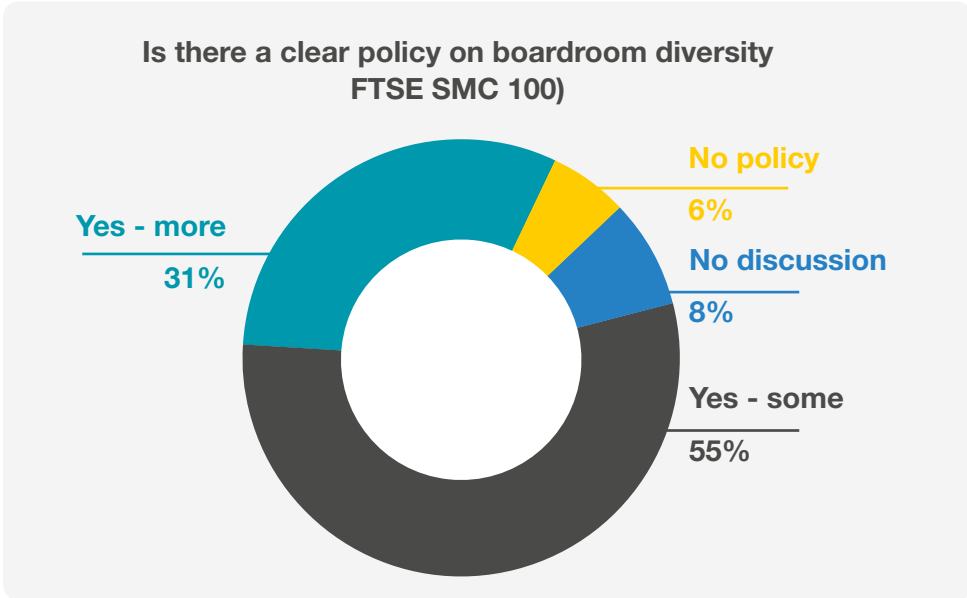
⁸ These categories are broadly consistent with the methodology employed by the FRC and University of Exeter in their review of Diversity Reporting in 2018.

Perhaps unsurprisingly, those companies in AIM that follow the UKCGC rather than the QCA code (38% of the AIM UK 50) are slightly more likely to have a clear board policy on diversity. This suggests that the regulatory pressure - even in a comply or explain format - is a driver for change. However it still means there are companies failing to meet the requirements of the UKCGC.

A fifth of companies in the AIM UK 50 have a policy that explicitly mentions board ethnic diversity. Only two mention it as part of their director succession planning, and none set any measurable objectives. Four companies mention initiatives they have for increasing ethnic diversity at senior management level, although none of them demonstrated meaningful commitment to these initiatives (for example including targets or periodic review.)

FTSE SMC 100

Reporting on diversity in the FTSE SMC 100 is generally better than in the AIM UK 50, and largely in-line with that of the FTSE 250⁹, again suggesting regulatory pressure makes an impact. 86% have some description of an approach to boardroom diversity. Another 6% explicitly state that they do not have a policy on board diversity, and that they recruit based on merit or on skills and experience. Eight percent have no mention of diversity at all, failing to meet the requirements of the Code.



⁹ Board Diversity Reporting, September 2018. <https://www.frc.org.uk/getattachment/62202e7d-064c-4026-bd19-f9ac9591fe19/Board-Diversity-Reporting-September-2018.pdf>

More than half (55%) only provide relatively minimal or boiler-plate descriptions; for example by stating that their policy on board diversity is that “the Board should have a broad range of skills, and that consideration is given to the recommendations of the Code and other guidance on boardroom diversity”. Nearly a third (31%) provide extra detail. These companies for example states that “we believe that it is in the interests of shareholders that board appointments are made on the basis of merit but also believe that there are substantial benefits to be had from having a Board composed of a diverse range of individuals, who are able to contribute to boardroom deliberations from different perspectives”. These proportions are almost identical to the FTSE 250 in 2018, where 58% of companies had a simple or basic gender diversity policy and just over a third provided more detail.

42% of FTSE SMC 100 companies mention that gender or ethnicity is a factor in director succession planning, although some of these only include a cursory mention. Just eight companies set measurable objectives for gender diversity at board level. Nearly a quarter (24%) mention that diversity is part of the board evaluation process - an encouraging proportion but one that could be much higher.

It is notable that while 86% of the FTSE SMC 100 explain their approach to gender diversity, only 46% actually describe this as a board diversity policy, despite reporting requirements stating companies should have a diversity policy. We found many companies which, for instance, state they do not have a formal board diversity policy but also state that when they recruit directors they pay regard to the need to have a diverse board, and also report on that diversity. This may then suggest a confusion in reporting, where boards assume a Diversity Policy is synonymous with setting diversity targets.

Given that under the requirements of the Code (and for the FTSE SMC 100, the FCA’s Disclosure Guidance and Transparency Rule 7.2.8A), companies have to describe their “diversity policy” or explain why you don’t have one, it is concerning to see such patchy reporting and such reluctance to develop or report on a clear policy, even when they do clearly have an approach to diversity.

It is also common for companies to have statements about board diversity spread across three or more sections of the annual report, and in some cases having contradictory reports - stating in one section that they do not have a policy and then in another that they do. This confusion makes it difficult to identify those companies that are not supportive of diversity from those who have considered it but are not effectively reporting on it, making accountability difficult to ascertain.

Methodology

This review covers the companies in the AIM UK 50 Index and the 100 largest companies in the FTSE Small Cap Index as at 30 September 2019. The data was collected from the companies' latest annual reports, published up to and including 31 October 2019. Given that some of the annual reports had been published up to 11 months previously (and that they can be out of date by the time they are published) we also reviewed appointments made between the date of publication of the annual report and 31 October 2019 using Companies House data and companies' regulatory announcements and websites, to get an up-to-date picture of the board. We excluded any companies registered outside the UK, to ensure a certain level of non-financial information in their annual reports.

Data on gender and ethnicity of directors was gained from companies' reporting. Ethnicity, where not reported, was assessed using the same methodology as the 2017 Parker Review¹⁰, which is an exemplar in this area. As they also acknowledge, assessment of people's ethnicity and race is not always clear cut, and the language used to describe directors' ethnicity is also imperfect. Nationality and country of residence was obtained from Companies' House data and companies' annual reports.

We used the same methodology as the Parker review in our assessment of directors' ethnicity. We are also aligned with the Parker review in our use of the term 'directors of colour', namely that there is no noun/group of nouns would be perfectly suitable to capture this, and we use the broad term "people of colour" to capture individuals with evident heritage from African, Asian, Middle Eastern and South American regions. We also use the term "non-white" directors in this report, but acknowledge the imperfections inherent in defining any group of people by their relationship to whiteness.

We also reviewed the quality of diversity reporting of these companies. This analysis followed a similar approach to the review by the FRC and the University of Exeter into board diversity in the FTSE 350¹¹, which looked at how companies discuss diversity in their annual reports. We looked for references to diversity throughout the front end of the report, looking for references to diversity policies or initiatives. The quality of reporting in these areas was addressed using the same categories and description. Our data was cross checked by two researchers to ensure consistency in the judgment of reporting quality.

10 Diversity of UK Boards – Sir John Parker, The Parker Review Committee (November 2016)

11 Board Diversity Reporting – FRC and University of Exeter Business School (September 2018)

Company Matters



Dr Scarlett Brown

Corporate governance and diversity consultant

Scarlett is a social researcher, using insights to encourage better practice in business. She's always had an interest in board diversity and director recruitment, and her previous roles involved giving research insight and advice in governance trends and best practice. Scarlett's now head of research at Tomorrow's Company, a non-profit think tank that helps businesses become a force for good in society. She's also co-founder of NED-recruitment platform Dynamic Boards, and is a trustee and NED.



Caroline Emmet, ACIS

Senior technical manager
Company Matters

Caroline leads Company Matters' technical team and technical committee. Together, they keep colleagues up-to-date on regulatory, legal and governance developments, as well as good practices that are relevant to a company secretary's core duties. The team considers the impact on their different client types, including FTSE 350, Small Cap, AIM, operating/commercial companies, investment trusts and larger private companies. With a background in investment banking, Caroline is well equipped to support Company Matters' array of clientele.



Paul Johnston

Senior consultant
Company Matters

Paul supports and oversees the function of our company secretarial business that is outsourced by clients, including board and committee support, compliance, and advice on good corporate governance practice. He also helps develop the knowledge function of the Company Matters team that supports colleagues in giving the best possible advice to our clients. Paul's clients range from premium-listed to AIM. Before joining Link, he led the secretariat team in a national charity, and he holds a master's degree in corporate governance.

Company Matters is a trading name of Link Market Services Limited, a company within the Link Asset Services group of companies. Link Asset Services is a trading name of companies which offer a range of services, principally shareholder, treasury management, fund and corporate administration services and related products.

All of the companies operating under the Link Asset Services trading name are wholly owned subsidiaries of Link Administration Holdings Limited, a company incorporated in Australia and listed on the Australian Securities Exchange. Company registered address Level 12, 680 George Street, Sydney, NSW, 2000, company registration number 120964098.

For more information on the Link Group, please visit www.linkgroup.com