

The role of a non-executive director in SMEs: Engage SMU profs

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Q: I am an executive director of an SME. Should I follow the best practices of the Code of Corporate Governance to employ some non-executive directors? What is the role of a non-executive director in an SME? Where do I find a non-executive director?

A: The Code of Corporate Governance issued by the Monetary Authority of Singapore (MAS) and the Singapore Exchange (SGX) not only outlines the best practices for public-listed companies, but also sheds light on governance and operating issues in private SMEs.

Unlike public-listed companies (usually the larger ones), smaller firms typically have negligible conflict of interest between the owners and managers, because the owners are often managers themselves. In small and even medium-sized businesses, it is relatively uncommon that a formally constituted non-executive director sitting on the board would be able to add value in any meaningful way.

Owner-managers may feel that an "outsider" non-executive director would cause disruption to the management of the company (due to his/her unfamiliarity with the business), or create unease among the board members when discussing strategies or issues of confidentiality.

To the best of my knowledge, I do not know of any SME in Singapore which employs independent non-executive directors. Even in a more advanced economy such as the UK, only 40 per cent of medium-sized companies employ non-executive directors.

However, as your business grows, you should be made aware of the immense benefits that a non-executive director can bring to your company and make plans to bring one or more on board to take your business forward.

In a public-listed company, independent non-executive directors are expected to play the role of a "watchdog" to monitor the non-owner managers. In most owner-managed SMEs, non-executive directors should be recognised as "management advisers" who can bring benefits in terms of their knowledge, experience and alternative perspectives.

They are even more committed than external professional consultants because they will be regarded as part of the management team. Especially for young entrepreneurs, non-executive directors can broaden their horizons and experience that they would not normally obtain within a short time, or might not be able to afford to engage external consultants.

Non-executive directors could help you secure more funding by adding credibility to your management team. They may also bring private-equity investors or venture capitalists to purchase shares in the business.

Experienced non-executive directors may have important and useful contacts who could help one to understand the market and gain more customers. Another vital role they can play is to evaluate and comment on the company's investment plans, especially at critical stages of the business.

A lack of experience at top-level management could hamper business growth or slow it down. Hence, as your business expands, you need to review periodically the expertise mix of your management team. A good team of executive and non-executive directors should be made up of people from different backgrounds and with different types of expertise.

You should look for non-executive directors who are able to bridge the gaps in skill sets or areas of expertise not available in your existing team of executives. In a larger SME, for example, a team of non-executive directors could comprise:

- At least one director who has had wide experience of leadership and strategic planning of a company;
- A director with niche expertise, such as sales or marketing, human resources or technical know-how of the mainstream business;
- A director with good government connections; and/or
- A qualified accountant or lawyer.

Besides leadership and niche expertise, I strongly believe that it is useful for non-executive directors to have government connections and proficiency in financial and legal matters. As we all know, a good relationship, or *guanxi*, with officials is extremely important for doing business in Asia - particularly in China.

Some entrepreneurs may have limited financial or legal knowledge and have difficulty in grasping issues pertaining to budgeting, financial or investment analysis, as well as business contracts. An accountant or a lawyer could help the executives examine management, tax or legal issues and their implications from a different angle.

There are some who believe that a gender-balanced board may perform better than one that consists solely of males. However, one should bear in mind that it is the niche business knowledge and the network of professional contacts of any non-executive director that a company will find valuable, rather than other factors such as gender or age.

The chairman of a large Singapore bank recently remarked at a public event that his bank hired a female non-executive director not because she is a woman.

In other words, you need to find a person with specific expertise who can help you grow your business.

So, where can a good non-executive director be found? Before you start searching for a potential candidate, you need to consider what you hope to achieve. Are you looking for more clients to increase market share, penetrate a new market, enhance your business planning or just form a more credible management team?

Understand your needs and then identify the right type of experienced individuals who possess the necessary expertise or business networks. There is a high possibility that your "perfect" non-executive director may be someone you already know.

The person could be a well-known individual in your industry whom you could approach on a confidential basis. This person could also be someone whom you had worked with in the past, or a client who understands your business through and through and who has excellent contacts. Your relatives, friends or classmates could be potential candidates too.

You may also approach Spring Singapore and the Singapore Institute of Directors for recommendations. Another option would be professional headhunting firms which recruit non-executive positions for companies.

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