AUSTRALIAN INSTITUTE
of COMPANY DIRECTORS

SME Business Owners/Directors

Good governance – A roadmap for growth

Good governance practices can increase your company's long term viability, enhance the business' value and pave the way for growth

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> *"While good governance "looks different" for different sized companies the role it plays - not only in compliance but in risk management, business performance and sustainable growth - is critical for all."*
>
> **Andrew Douglas FAICD, Managing Director**
> **Nexus Executive Services Pty Ltd**

Some myths around instituting governance practices include: "governance creates more work", "it's going to cost a lot/ take too much time" and "a governance system is for big companies only."

The truth is very different. The basic principles of good governance are fundamental to the sustainability of all businesses whether they be small, medium, large, family owned, private or public companies. The creation of a business plan, building appropriate financial acumen, risk management, succession planning and ensuring there is accountability and transparency to owners are just a few of the vital components a successful enterprise.

As a business owner/director of a small to medium business, it is important to understand your role in the growth of the business and the positive impact that good governance contributes to this growth.

What is corporate governance?

To oversee business and compliance performance, business owners/directors (and in turn, boards) must put in place a system of processes to communicate, control and monitor (or 'govern') the organisation.

Another way to look at it is that governance "brings the right people together at the right time to discuss the right (important) things." *John Davis, Governing the Family Run Business HBSWK Pub. Date: Sept 4, 2001*

Good governance for business growth

If you are the owner of a small to medium business, you are probably also a director and possibly the manager. In the face of the different demands each of these roles bring, it's important that you don't 'lose sight of the forest for the tree's' - focusing a disproportionate amount of time on operations ('in the business'), rather than on the strategic growth ('on the business'). This is where governance can introduce discipline, providing a roadmap for the future.

Why governance is important to your business:

1. Business Growth
2. Performance Management
3. Risk Management
4. Compliance

1. **Business Growth:** There is a strong link between governance and the bottom line. Good governance practices encourages growth in the following ways:
   - **Increased business performance:** good advice, be it from advisors or a well structured board, contributes to the performance of the business and thereby increases the value of the company by: developing better strategy, advising and mentoring the owner or management, and providing the business with vital contacts or resources.
   - **Raising Capital:** a good track record of governance practices can be critical for attracting investment. Practicing good governance provides confidence to investors, financial institutions and venture capitalists.
   - **Financial Control:** managing your company's finances, including cash flow and debt management are critical factors for a growing company.
   - **Accountability:** the separation of management from control fosters accountability and is in the best interests of the company.
   - **Building relationships:** a strong track record of fair and transparent governance can also attract and retain good customers, suppliers, employees, etc.
   - **Competitive Advantage:** good governance practices help build sustainable competitive advantage and can give your company an 'edge'.

2. **Performance Management:** Building a strong foundation from a 'people perspective' and setting up the appropriate mechanisms to monitor and manage performance - particularly senior managers - ensures the owner/director's strategic intent is effectively translated into practice.

3. **Risk Management:** Understanding, assessing the risks to your business and building strategies to mitigate those risks is core to good governance. Failure to identify and mitigate risk can have a significant legal and financial impact to your business. For example, a risk may be 'maintaining the status quo' when the company needs to evolve, invest and grow to prosper, even in the medium term.

4. **Compliance:** Your company must comply with the rules and regulations required of a business registered under the Corporations Act (2001). Practicing good governance will ensure you have adequate processes in place to comply with all legal and accounting requirements, and that you have an understanding of your legal and financial obligations as a business owner/director.

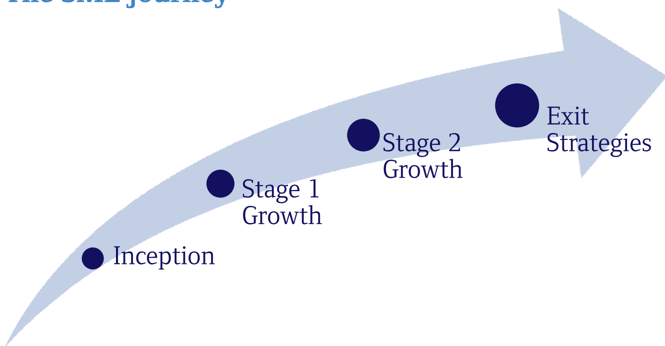
   It's important to note that the law will rarely, if ever, forgive business owners/directors for a breach of duty on the grounds that you are only a small business, or that you simply didn't know.

What core governance practices should I be considering for my business?

There is no universal formula for successful corporate governance. Businesses vary in size, complexity and ownership structures. As your small to medium business grows, the structure will need to evolve with your changing business needs.

The following "SME Journey" offers practical suggestions for governance structures during each stage of your business' growth.

The SME journey



A Scorecard for Growth

The development of businesses vary considerably from case to case, however there are some common stages:

Inception: Setting up the business

Governance begins when you incorporate your business. Incorporation provides a structure - as governed by the Corporations Act (2001) - and it means your business now operates in an environment where laws and third parties must be heeded. What you should be considering at a minimum:

- **Being a director:** understand your role, responsibilities and risks
- **Indemnity and insurance:** protection for legal liability as a business owner/director
- **Set up business planning:** create a simple strategic business plan
- **Build measurement:** build a simple set of key performance indicators
- **Idenfity risks:** analyse business risks and create a basic set of policies to mitigate these risks, including appropriate insurances
- **Engage external advisors:** these can be an invaluable source of professional advice
- **Develop reporting requirements:** create a system to monitor performance and keep best practice financial records
- **Create a succession plan**

Stage 1 Early growth

Your business has now grown – either in employee size or revenue – and you want to continue growing over the next 3-5 years, you should consider:

- **Set up formal structures:** such as formal accounting systems, simple policies for HR, remuneration frameworks and policies for purchasing and sales
- **Raise funds:** through financial institutions or investors
- **Develop strategic partnerships:** to access new markets
- **Create growth strategies:** a detailed 3-5 year business plan and annual review
- **Enhance your measurement:** using a number of key performance indicators and appropriate budgeting systems
- **Continue to manage risks:** institute formal systems to manage risk
- **Establish an advisory board:** for independent business advice and strategy
- **Increase your reporting requirements:** create a system to share the company's financial situation with all concerned
- **Institute performance management:** provide key players and managers with direction and create accountability
- **Develop succession planning:** involving formal business agreement.

Stage 2 Established growth

You now have an established business. Your business has several shareholders and/or partners and you now require a more robust system of governance practices that should include:

- **Create a board:** to set goals and strategies for the company
- Appoint external directors to the Board
- Establish a mechanism to ensure board performance
- Build an extensive network of policies, measurement and reporting systems
- Increase reporting requirements: understanding financial reporting (Australian Securities and Investment Commission (ASIC) Financial Reporting) for revenue and employee thresholds, etc
- Develop an established model and history of good governance

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Exit strategies

At some point you may choose to exit the business, and/or go public. If your plan is to exit you should consider:

- Prepare for an initial public stock offering (IPO), a merger/acquisition with another company or taking on an equity partner
- Enact a trade sale
- Consider reporting requirements: for publicly listed companies, as required by ASIC and the Australian Securities Exchange (ASX)
- Execute the succession plan: prepare your successor to 'take the reigns'

Who is involved in governance?

The people involved in or impacted by governance practices include:

- Business owners
- Directors and boards
- Managers
- Employees
- Shareholders and/or members
- Auditors
- Other stakeholders such as suppliers, partners, creditors and customers

Some individuals, of course, have multiple roles.

Good governance will only work in your business if individuals responsible for undertaking actions on behalf of the company understand, abide by and embrace the principles of good governance as part of the company culture.

To learn more

Visit **companydirectors.com.au**, for further SME resources such as:

- Online SME Guides – for more information about how good governance can help you grow your business see our other online guides for SME business owners/directors:
  - Introduction to the owner/director's role in growing their small to medium business
  - The benefits of an advisory board – mentoring for growth
  - The benefits of a board
- Articles
- Video: Kochie's Business Builders, Interview with Brand Hoff, 15 November 2009
- Frequently Asked Questions (FAQ's)
- Director and Board Education Courses – including:
  - Foundations of Directorship Course – available for directors of small and medium companies
  - The Role of the Director – an e-learning course
  - Company Directors Course – a comprehensive program for directors
- Events, books and other information to support you in your strategic role as a director

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