



The Idea Of A “Professional” Independent Director

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Introduction

The institution of the independent director continues to play a vital role in corporate governance. Although it has been subjected to some level of criticism, particularly in the aftermath of various corporate governance scandals unearthed from time to time, its importance has been undeterred. Anecdotal evidence of this phenomenon is aplenty. Recently, independent directors of companies affected by financial improprieties and wrongdoings have taken on a frontline role to revive and resuscitate such companies and thereby protect the interests of the public shareholders. The Sino Environment case is one such example. Regulators too are pinning greater hope and responsibility on independent directors. SGX’s recent proposal that requires offshore principal subsidiaries of listed companies to have at least one Singapore-resident independent director is emblematic of this trend.

All this leads to the crucial question as to whether independent directors are well-positioned to undertake such demanding responsibilities. In an era of increased complexity in business transactions and uncertainty in the business environment, independent directors are not only required to possess exceptional business expertise and acumen, but they are also required to devote substantial amounts of time and attention to the affairs of the boards on which they sit.

Currently, independent directors are typified by business executives such as CEOs and senior managers of other companies, or by professionals such as lawyers, accountants and consultants, or by government officials or academics. These are individuals with primary ‘day jobs’ for whom the independent directorship of a company is but one of many tasks. They devote only a certain number of days a year for board responsibilities. Prior to board and committee meetings, they are required to plod

through reams of reports and other information, which are often technical as well as plentiful. When a company is performing well, the independent directors tend to adopt a more tolerant approach towards management in the absence of any 'red flags'. However, when a crisis situation emerges, they are compelled to be at the forefront and take charge of the affairs of the company. Can independent directors be relied upon to avert crises in the first place? Arguably not, if their role in the affairs of the company is minimal as it currently is.

The Concept Of A Professional Director

In these circumstances, it is worthwhile to consider the concept of a 'professional' independent director. Although the idea, which was conceived a few decades ago, has not yet received the momentum it deserves, the ever-increasing demands on independent directors merits its reconsideration. Joseph Barr defines a 'professional director' as "a man ... who spends all his time in the discharge of his responsibilities as a director of various publicly held corporations". Such an individual embraces independent directorship as a profession to the exclusion of all else. This idea was subsequently popularised by two U.S. law professors who argue that this class of directors would possess the skill, time and necessary incentives to more ably perform the role of independent directors.

Let us now consider the broad contours of such a position. Under this scheme, each board may have one or more professional independent directors in addition to conventional independent directors as well as executive directors. The most appropriate candidate for professional directorship would be a retired senior business executive, or a partner at a law firm or accounting firm, or a leading academic in business or other relevant discipline. Such an individual, who possesses the requisite expertise and experience, would commit all his time and energy to being an independent director on various boards. It is necessary to ensure that there is a limit placed on the number of such directorships an individual may hold. Imposing a maximum of five to six directorships seems suitable.

Advantages

A distinct advantage of this option is that it allows such individuals to focus their attention exclusively towards performing their directorship roles efficaciously in companies on whose boards they sit. As they are not distracted by any other principal

occupation, they can spend greater amounts of time and attention towards the companies' affairs. It enables greater interaction with managements of companies (at various levels) resulting in a smoother flow of information to the board, and more specifically the independent directors.

Apart from these professional directors being experts in their own right, they can potentially benefit from participating on boards of several companies. They can enrich themselves by learning from their experiences on one board, and then apply that on other boards, thereby resulting in a cross-fertilisation of ideas and best practices. This generates an optimal outcome for all the companies on which the individuals are directors.

Appropriate incentives are to be made available to the professional directors so that they undertake their role with earnestness. They have to be adequately remunerated by the companies, either through salaries, stock options or other recognised perquisites. At the same time, care must be taken to ensure that the remuneration is not so excessive as to impinge upon the independence of the directors. In other words, the directors ought not to be beholden to management. Even in this respect, the proposal for professional directors presents an elegant solution. The incentive scheme would work such that the aggregate remuneration received by a professional director from all companies in which he holds a position can be comparable to what he was earning prior to adopting such a role that suitably motivates the individual to do a good job. But, the remuneration from each such company will not be so significant as to impair objective decision-making on the board.

Addressing Drawbacks; Defining The Role

The introduction of a professional independent director is not without drawbacks. First, it would be a daunting task to identify a sufficient number of individuals with the requisite competency to adopt such a role by giving up their existing occupations. Second, companies and their managements may be averse to the idea as professional directors may tend to act as super-monitors and interfere in the day-to-day functioning of companies. Some of these constraints can nevertheless be addressed. As regards the first concern, it is not as if every independent director should satisfy these characteristics. The professional director will be a minority in each

company, and considering that each individual would be occupying positions in other companies as well, the number of such individual required would not be significant. As for the second concern, that can be alleviated by carefully carving out a role for the independent director, a matter to which I now proceed.

It is recommended that the role of independent directors consist of two parts: (i) advisory; and (ii) monitoring. Independent directors need to bring value to the company in terms of their ability to provide inputs on strategic, business, marketing, legal, compliance, or other relevant aspects, and also carry out monitoring functions (by acting as watchdogs) in order to protect the interests of shareholders. These roles are to be clearly outlined so that independent directors are not subject to any uncertainty on this front. Admittedly, it may be a tall order to require every independent director to perform both advisory and monitoring functions, and that may not be practicable to begin with. However, the board could be comprised of independent directors with different capabilities so that the board as a whole may be in a position to perform both these functions effectively.

The next key issue pertains to the constituencies that deserve the attention of independent directors. In countries such as the U.S. and the U.K., where shareholding in companies is diffused, the shareholder body is homogenous and hence independent directors can merely take into account shareholder interest as a common factor. However, in countries such as Singapore where shareholding is

generally concentrated, the shareholder body itself would be bifurcated into two distinct interests, being that of the controlling shareholders and of the minority shareholders. Since controlling shareholders are in a position to exercise some level of dominance over a company's affairs by virtue of their voting power, independent directors would have to specifically cater to the interests of minority shareholders. If independent directors (whether of the professional type or the conventional type) are to play a meaningful role in corporate governance, some of these roles and functions have to be better clarified.

The Way Forward

As for implementing the professional independent director concept, the way forward would be for companies to identify such individuals and begin engaging with them. Once its success is determined in a few companies, it can be expanded to others. It is advisable to introduce this requirement as a matter of best-practice rather than through regulatory intervention or through imposition as a matter of law. This process can be aided through effective utilisation of directors' databases and exchange of information. Thus far, we have not considered the concept of a professional director as requiring some sort of registration or accreditation with a suitable professional or peer body. In due course, it may augur well to implement such a system accompanied by training (both initial and continuing) that would inculcate an innate sense of professionalism in the institution of the independent director. ■

References:

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