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The Perception of SMEs towards the Corporate Governance in Malaysia

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ABSTRACT

Today's industry players, regulators, investors, and researchers agree that boards of directors play an essential role, and this consensus has led to widespread recognition of the significance of this role. Since the financial crisis in 1997 and 1998, researchers in Asia have begun to focus on this topic. Guidelines for effective corporate governance practices have been developed and published by several developed and developing nations and international organizations. On the other hand, most of the policies focus on publicly traded companies rather than small and medium-sized businesses (SMEs). There is a requirement for an excellent corporate system to be in place in any organization, regardless of its size, to ensure transparency, accountability, and the disclosure of all relevant financial information. This is necessary to keep the organization in a state of equilibrium. This research examines the perception of small and medium-sized enterprises (SMEs) regarding the crucial role of governance in business and their assessment of the significance of different duties and responsibilities assigned to boards of directors. Given the substantial impact of boards of directors on the success of businesses and the contribution of SMEs to the growth of the Malaysian economy, understanding SMEs' perspectives on governance is essential. The researchers developed the questionnaire based on prior research and existing corporate governance guidelines. Random sampling was used to collect data for this study. Two thousand questionnaires were handed out, but only 1,449 small and medium-sized businesses (SMEs) filled them out. The findings indicate that SMEs are aware of the critical role of corporate governance players and the responsibilities that come with that role. On the other hand, the regulators need to devise effective corporate governance practices for SMEs.

Keywords: Corporate governance, Board of Directors, Shareholders and SMEs and Malaysia

1.0 INTRODUCTION

Due to the Asian financial crises (Johnson, 2013; Hawley et al., 2011) and corporate failures such as Lehman Brothers (Kumar & Singh, 2013), the significance of corporate governance (CG) has been emphasized if its history is revisited. Cadbury Report from the United Kingdom in 1992 established the first CG guidelines (European Corporate Governance Institute, 2013). Following that, a multitude of developed and developing countries, as well as international organizations, implemented corporate governance guidelines to structure the board of directors. This indicates that regulators, industry participants, and investors are recognizing the significance of the board of directors in providing guidance and counsel to companies, enabling them to achieve profitability and sustainability while fulfilling their corporate social responsibilities. The importance of a robust corporate governance system in facilitating recovery

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from financial crises, promoting sustainable growth, instilling investor confidence, and mitigating the risk of mismanagement has been widely recognized.

Incorporating CG principles can result in positive outcomes for the owners and managers of the business (Vicente-Ramos et al., 2020;Süsi& Jaakson, 2020; Jan et al., 2021; Teixeira & Carvalho, 2023; Garzón, 2021; Sarhan & Al-Najjar, 2023; Farooq et al., 2022). At the same time, this will improve the information's accessibility as well as its level of transparency. Because of this, businesses can more easily gain access to additional capital and attract partners and investors. According to Rachagan&Satkunasingam (2009), it will also contribute to the enterprises' ability to survive and sustain themselves in an increasingly competitive situation by facilitating mergers, acquisitions, and partnerships. On the other hand, all of the existing CG codes focus on publicly traded companies rather than small and medium-sized enterprises (SMEs). Only a select few nations, including Hong Kong, Dubai, and the OECD, have established guidelines for corporate governance in SMEs. Compared to SMEs, publicly listed companies have more differentiation between ownership and management than other businesses. This could be the cause of the observed phenomenon. However, in today's world, due to the complex nature of businesses, the rapid growth of SMEs, and the fact that these businesses should be aware of the critical role that CG plays in their operations (Wanjohi et al., 2010).

Barnes (2013) demonstrates that it is essential to understand the type of corporate governance appropriate for small and medium-sized enterprises (SMEs). According to Neville (2011), who investigates the ownership and control structure of 1,313 small and medium-sized enterprises (SMEs) and conducts an interview survey of 1,040 Danish owner-managed SMEs, the role of the board of directors ought to be more focused on resource suppliers than controllers. According to the findings of Umrani et al. (2015), there is a conflict of interest between majority and minority shareholders in Malaysian SMEs. The situation becomes even more dire in Malaysian SMEs that have concentrated shareholdings. They have suggested that good corporate governance should be in place to control and monitor SMEs to guarantee that all parties' interests are served just and fairly. There is a significant possibility that Malaysia's small and medium-sized businesses will propel the country's economy forward. In addition to their controlling and monitoring responsibilities, researchers believe that boards of directors should also play an advisory role in the guidelines for small and medium-sized businesses' corporate governance. This would require a different approach than the current one. According to Hamad and Karoui 2011, there has been a paucity of research on the relationship between corporate governance and SMEs. To our knowledge, little research has been conducted to investigate how small and medium-sized enterprises in Selangor, Malaysia, view the role boards of directors play. As a result, this study aims to investigate the attitudes held by small and medium-sized enterprises (SMEs) regarding the vital part played by the board of directors in sound corporate governance.

2.0 SMES AND CORPORATE GOVERNANCE

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A company falls into the small- to medium-sized enterprise (SME) category if its revenues, assets, or employee counts are below a specific threshold. A small or medium-sized enterprise (SME) definition varies across countries and industries. Regrettably, a universally recognized definition for a small and medium-sized enterprise (SME) does not exist. Each sovereign state has the authority to establish its interpretation and may also enforce specific limitations on specific areas of activity.

For instance, the European Commission defines a small and medium-sized enterprise (SME) as "An enterprise which employs less than 250 people; has an annual turnover of less than €50m and balance sheet assets of less than €43m; and has no more than 25% of its capital or voting rights owned by a larger firm or public body." In the United States of America, a small to medium-sized enterprise (SME) can have up to 1,200 workers (Nugent &Rhinard, 2015).

However, a key objective of defining what qualifies as an SME is differentiating between small and medium-sized businesses and large corporations. This objective aims to accomplish this by contrasting the sizes of small and medium-sized enterprises with those of corporations.

Small and medium-sized businesses comprise most companies in most nations. The Small Business Administration (SBA) estimates that 99.9% of businesses operating in the United States in 2018 were considered small businesses. According to the Small Business Administration (SBA), small businesses were responsible for approximately 44 percent of the gross domestic product in 2014 (the most recent year for which data was available). Even though this proportion of GDP has shrunk since the 1990s, small and medium-sized enterprises (SMEs) continue to play an essential role in the economy's expansion, innovation, and diversity.

Corporate Governance systematically analyzes the reasons behind companies' governance structure and practices (Del Gesso & Lodhi, 2024; Assfaw, & Sharma, 2024; Bhatia & Kumari, 2024). It discloses the individuals who hold positions of authority, are responsible for making decisions, and possess the power to make decisions. At its core, it is a set of tools that empowers management and the board of directors to address the challenges of company operations effectively. Corporate governance establishes effective mechanisms and protocols to achieve a harmonious equilibrium among the diverse interests of stakeholders, encompassing shareholders, employees, suppliers, customers, and the community (Cardoni et al., 2024; Feng et al., 2024; Ahmad, 2024; Bolatito & Mohamoud, 2024; Huang et al., 2023; Zhang et al., 2023; Li et al., 2018).

Corporate governance encompasses the procedures a company employs to establish its objectives and subsequently strive towards attaining them, considering the social, regulatory, and economic landscape in which it functions. This pertains to the methods and protocols implemented to ensure that a company operates in a manner that allows it to accomplish its goals

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while also instilling a sense of trust and confidence in its stakeholders. The term "achieving its objectives" pertains to the company's aims.

The researchers assert that good governance is crucial as it establishes the framework necessary for enhancing the caliber of decisions made by business managers. The researchers assert that effective governance is crucial. Adhering to ethical standards and making high-quality decisions is crucial for businesses to achieve sustainability and enhance their ability to create long-term value.

2.1 The Importance of Corporate Governance in SMEs

In contrast to large corporations, many small and medium-sized enterprises (SMEs) do not clearly distinguish between management and ownership Tumaku & Agbeko, (2024). On the other hand, this does not imply that good corporate governance is not essential. Even the most fundamental corporate governance structure can benefit a small or medium-sized enterprise (SME), particularly if the business has expansion goals. The capacity of a company to acquire additional funding from outside sources, and consequently, its capacity to expand, can be significantly bolstered by implementing an effective governance system. Companies that are effectively managed and have sound systems in place are more likely to attract lending capital from investors, who are also more likely to pay a premium price for shares in those companies.

The management of the company and its operations will improve if the company's roles and responsibilities are well-defined and its internal procedures are straightforward to understand. Everyone who has a stake in the company, from management to shareholders to other stakeholders, will clearly understand how the company functions. It allows management to concentrate on the growth strategy and profitability of the company, which is beneficial for owner-managed small and medium-sized enterprises (SMEs) because it lowers the risk of internal conflicts. A well-structured and regular meeting board is crucial for small and medium-sized enterprises (SMEs) to discuss and plan the company's long-term strategy effectively. External non-executive board members can be highly beneficial in specific situations, as they bring additional expertise and supervision while counterbalancing the executives' perspectives. This ultimately leads to improved strategic decision-making.

Corporate governance does not attempt to eradicate risk or stifle creativity and innovation. Instead, the business is positioned to recognize, monitor, and reduce the risks it faces because it has risk management processes in place, which are supported by internal controls. Knowing that these will be managed appropriately makes it possible for the company to confidently embark on new initiatives (such as developing new products, joint ventures, or other collaborations). Suppose a business already has robust governance systems in place. In that case, there is a lower chance that those systems will fail, which increases the likelihood that the business will sustain reputational damage. The practice of good governance in a small or

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medium-sized enterprise can be a selling point and should be publicized to stakeholders and the outside world.

The long-term value of a company and its potential for expansion can be increased by ensuring that it has strong corporate governance. Corporate governance has critical benefits, including reducing risk and strengthening reputation, which are essential reasons small and medium-sized businesses cannot ignore its importance (Dhingra & Dwivedi, 2024; Jaroenjitrkam et al., 2024; Makpotche et al., 2024)

3.0 RESEARCH METHODOLOGY

This study employed both primary and secondary sources of information. Questionnaires are employed for gathering primary data, while secondary data is acquired by examining pertinent articles, books, and online resources. As far as we know, no research has been conducted on corporate governance, specifically for small and medium-sized enterprises (SMEs). This study aims to examine the topic by utilizing a questionnaire to assess the perception of small and medium-sized enterprises (SMEs) regarding the significance of the primary duties of boards of directors as corporate governance (CG) participants. The survey aims to collect data from small and medium-sized enterprises (SMEs) regarding their viewpoints on the functions and obligations of boards of directors, the makeup of boards, and the autonomy and dedication of board members. Furthermore, this study delves deeper into the viewpoints of small and medium-sized enterprises (SMEs) regarding directors' oversight responsibilities in financial reporting, risk management, and monitoring the company's relationship with its shareholders. We employ a five-point Likert scale ranging from strong disagreement (1) to strong agreement (5). The questionnaire is collected using a stratified sampling method. Figure 1 displays the overall quantity of small and medium-sized enterprises (SMEs) in Selangor, Malaysia.

Figure 1: SME Profile: Selangor

Sector	Name of SME establishments	Percentage
Agriculture	732	0.2
Mining & Quarrying	120	0.1
Manufacturing	9,530	5.3
Construction	7.606	4.2
Services	161,283`	90.0

Sources: Invest Selangor, DOSM's Socioeconomic report 2021, and SME Bank SCEA

4.0 FINDINGS

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A total of 2000 questionnaires were handed out, and 1499 small and medium-sized businesses responded. Therefore, the percentage of people who responded was 74.95%. Most respondents are men, accounting for 61.55% of the total. The respondents' educational backgrounds show that most have at least a bachelor's degree, followed by those with diplomas, holders of other qualifications, master's degrees, and those with professional qualifications. In addition, most respondents work in the service industry, followed by those in the construction industry, manufacturing and agriculture, and mining and quarrying. Regarding age, the vast majority of respondents are between 40 and 49. In terms of their experience in the workforce, the vast majority of respondents have between 6 and 10 years of experience.

Table 2: Profile of Respondents

	Frequency	**Percentage**
Gender		
Male	892	61.55
Female	557	38.44
Total	***1449***	***100.00***
Educational background		
Diploma	292	20.15
Bachelor degree	692	47.75
Master	189	13.04
Professional qualification	42	2.89
Others	234	16.14
Total	***1449***	***100.00***
Sectors		
Agriculture	50	3.45
Mining & Quarrying	42	2.89
Manufacturing	234	16.14
Construction	286	19.73

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Services	837	57.76
Total	***1449***	***100.00***
Age range		
20 – 29	89	6.14
30-39	539	37.19
40-49	723	49.89
50-59	143	9.86
60 and above	5	0.34
Total	***1449***	***100.00***
Experience with small and medium-sized enterprises		
Below three years	249	17.18
3 – 5	240	16.56
6 – 10	378	26.08
11-15	325	22.42
16-20	220	15.18
21– 25	22	1.51
Above 25	15	1.03
Total	***1449***	***100.00***

4.1 SME Opinions Regarding an Overview of Corporate Governance

Table 3: SME Corporate Governance Code: An Overview

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S. No.	Description	Mean
1	It is necessary to develop a specific corporate governance code (CGC) that is customized to suit the requirements of small and medium-sized enterprises.	4.90
2	SMEs should be required to implement CGC.	4.81
3	The CGC should clearly define the roles and responsibilities of the board and management.	4.00
4	The CGC must possess sufficient adaptability to fulfill the requirements and meet the expectations of small and medium-sized enterprises (SMEs).	4.44
5	CGC should assign directors advisory roles in addition to their responsibilities as providers of strategies and monitors.	4.75
6	Most board members should consist of individuals the company does not employ.	4.60
7	The minimum number of board members should be three, and the maximum number should be seven, depending on the complexity of the business.	4.77
8	The majority of board members must maintain independence from the organization's management.	4.80
9	The SME should determine any division of responsibilities between the Chairman of the Board and the General Manager or Chief Executive Officer.	4.81
10	Board members should be knowledgeable and experienced in the SME businesses they are involved in.	4.77

Initially, we examine the sentiments of small and medium-sized enterprises regarding the comprehensive overview provided by the CGC. The mean value of 4.90 indicates a strong agreement among respondents that SMEs need customized CGC that meets their specific needs and that compliance should be mandatory (mean = 4.81). The respondents unequivocally support the notion that the code should clearly outline the roles and responsibilities of the board, as indicated by the mean value of 4.00 for this particular response. The idea that the role of the board of directors should be seen as advisors, in addition to being providers of strategies and monitors, is supported by the finding that the mean value of 4.75 from the statement asking about

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this role supports this notion. The majority of respondents hold the view that the company should not employ board members. Additionally, the average number of respondents (4.60) believe that board members should maintain independence from the management. A considerable proportion of participants express strong support for the notion of the board's autonomy. Furthermore, the average value of 4.81 suggests a significant need for segregating the CEO and Chairman of the Board roles. Because small and medium-sized enterprises (SMEs) are not as large as publicly listed companies, the board size must be reduced.

4.2 SMEs' Opinions on the Duties of the Board of Directors

Table 4: The duties of the Board of Directors

S. No.	Description	Mean
1	The Board of Directors convenes regularly to fulfill its governance obligations and ensure the effective functioning of SMEs.	4.58
2	Board members are capable of guiding SME risk mitigation.	4.73
3	Directors should participate in the risk management activities of SMEs.	4.79
4	The board should assess and improve the efficiency of the SME risk management team.	4.61
5	Board members are responsible for providing a timely and accurate view of the financial statements.	4.79
6	The details regarding board members include their compensation, the frequency of board meetings, and their background.	4.93
7	The annual report should comprehensively account for the fees paid to external auditors for audit and non-audit services.	4.84
8	The annual report should incorporate both internal control and risk management strategies.	4.78
9	The structure of shareholders should be detailed in the annual report.	4.84
10	The annual report must provide transparency by revealing the accounting policies, significant occurrences, and	4.59

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	potential liabilities.	
11	The annual report must emphasize the financial and non-financial performance over a minimum of five years.	4.49
12	The annual report should encompass financial statements from two consecutive years to facilitate comparison.	4.91
13	SMEs' future outlook should be included in the annual report.	4.78
14	Board members should exert maximum effort to effectively accomplish the goals of SMEs, safeguard their reputation, and possess complete and immediate access to all information, documents, and records about SMEs.	4.65
15	When preparing a company's financial statements, board members should know the prevalent accounting standards applicable to SMEs.	4.50
16	In order to update their knowledge, board members must attend the training.	4.77
17	The annual report should highlight the SME's contribution to society and environmental stewardship.	4.77
18	The zakat and income tax payments should be detailed in the annual report.	4.50

According to the survey results, there is a strong consensus that boards of directors have a fiduciary duty to fulfill their role as the primary decision-makers for small and medium-sized enterprises (SMEs), as indicated in Table 4. This discovery was made during an investigation into the board of directors' accountability. Small and medium-sized businesses strongly advocate for regular board meetings, with an average value of 4.58. Small and medium-sized enterprises may require more frequent guidance and support from board members. The board highly advises that SMEs receive guidance to reduce risks (mean = 4.73), actively participate in risk management activities with other SMEs (mean = 4.79), and assess and enhance the efficiency of risk management teams within SMEs (mean = 4.61).

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Small and medium-sized enterprises (SMEs) are considered separate legal entities from their owners regardless of whether or not the owners are members of the same family. Hence, it is crucial to promptly and sufficiently disclose the information in the annual report to demonstrate the performance of small and medium-sized enterprises (SMEs) and fulfill the board's obligation to shareholders and other stakeholders. There is no suggestion that small and medium-sized enterprises (SMEs) should adopt the practices of publicly traded companies and create detailed annual reports. However, to provide investors with helpful and up-to-date information, it is necessary to disclose all of the information that is considered to be material. All the mean values are more than 4.

Concerning the disclosure of financial accounting information, it is strongly recommended that the accounting policies, significant events, and contingencies be included in the annual report. It is to be noted that all the mean values are more than 4.

Disclosure of SMEs' contributions to society and how they care for the environment is something that the mean value of 4.77 strongly recommends in the context of the discharge of corporate social responsibility. A mean value of 4.50 makes additional recommendations regarding the disclosure of zakat and income tax paid each year. In conclusion, the board's efforts to achieve the objective of SMEs while also protecting their goodwill ought to be elaborated upon in the annual report. In conclusion, it is possible to state that the board bears responsibility for all aspects of SMEs, including risk management, information disclosure, meeting obligations related to corporate social responsibility, and so on.

4.3 Perceptions of Board of Directors' Relations with Shareholders and Other Stakeholders among Small- and Medium-Sized Enterprises

Table 5: The Perspectives of SME Owners and Other Stakeholders on the Board of Directors

S. No.	Description	Mean
1	Small and medium-sized enterprises (SMEs) ought to initiate measures to encourage the participation of shareholders in general meetings.	4.67
2	Small and medium-sized enterprises (SMEs) must ensure that the information disclosure process is effective and that its partners and shareholders are treated fairly and with consideration for the preferences they have expressed regarding exercising their inspection rights.	4.56
3	The board ought to ensure that the workers are dealt with consistently with fairness and equity and that there is no	4.83

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	discrimination based on factors such as the employees' race, religion, or gender.	
4	The board should guide small and medium-sized businesses in conducting their operations to ensure continued success.	4.92
5	The board should steer small and medium-sized enterprises (SMEs) toward developing standard operating procedures (SOPs) for dealing with and managing customer relationships.	4.64
6	The board ought to formalize ethical standards using a code of conduct and ensure its standards are followed.	4.92
7	The board ought to steer SMEs towards establishing procedures in order to safeguard resources and distribute them in a manner that is both efficient and effective.	4.85
8	When making decisions, the board ought to take into account a variety of stakeholders in addition to the owners in order to guarantee that all of the parties are dealt with fairly and justly.	4.97
9	The Board ought to think about how small and medium-sized businesses (SMEs) can contribute to the improvement of the economy in Malaysia.	4.67

Because boards of directors serve as the shareholders' agents, they must fulfill the responsibilities delegated to them by the shareholders while also considering the stakeholders' requirements. Therefore, this section discusses what small and medium-sized enterprises (SMEs) anticipate from their boards of directors regarding communication with shareholders and other stakeholders.

There is a widespread consensus that board directors are also responsible for shareholders and other stakeholders. The weighted average of 4.92 pieces of evidence suggests that the board should offer advice and direction to small and medium-sized businesses regarding how to run their operations to maintain their success. In addition, the average value of 4.92 pieces of evidence suggests that the board should formalize ethical standards by using a code of conduct and ensuring its standards are adhered to When making decisions, the board ought to consider a variety of stakeholders, in addition to the owners, to ensure that all parties are treated fairly and justly. The mean value for this expression is 4.97.

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5.0 CONCLUSION

The findings indicate that small and medium-sized enterprises (SMEs) acknowledge the significant role and accountability of corporate governance stakeholders. The survey also indicates a requirement for implementing a comprehensive code of conduct for corporate governance in small and medium-sized enterprises (SMEs). This code would ensure that the board of directors acts in the owners' best interest while considering other stakeholders' needs. The findings of this study indicate that small and medium-sized enterprises (SMEs) require a corporate governance code (CGC) tailored to their specific requirements, and it should be mandatory for them to adhere to it. The respondents advocate for including specific details in the annual report, such as the frequency of board meetings and comprehensive and timely disclosure of information. This includes information about the board members and their service fees, including audit and non-audit service fees paid to external auditors. Additionally, they recommend including a statement on internal control functions, risk management strategy, zakat, and income tax. Regulators will be interested in these findings for the future formulation of regulations and their impact on medium-sized firms. This study serves as an initial investigation into the role of the board of directors in the SME sector. It is intended to lay the foundation for future research on governance mechanisms, practices, and financial aspects.

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