"OUTSIDE" DIRECTORS IN SME BOARDS: A CALL FOR THEORETICAL REFLECTIONS

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Abstract

Good governance for SMEs is critical for economic development and growth in both developed and developing economies. In this paper we focus on boards and governance in small and medium sized enterprises (SMEs) by investigating the role and contribution of "outside" directors in this setting. By contrasting board role theories against different types of SMEs, firms are expected to recruit "outside" board members for various reasons. Illustrated by 52 empirical studies of "outside" directors in SMEs we show how agency theory, resource based view of the firm, and resource dependence theory can be applied to understand the multiple roles that "outside" directors can play in family firms, venture capital-backed firms and other SMEs. The illustration shows that the concept "outside" director is not the same in different theories and in different empirical settings. Based on this finding, we argue for the need to have a conscious and balanced use of theories for understanding the role and contribution of "outside" directors in SMEs.

Key words: Boards of directors, outside directors, SMEs, family firms, venture capital

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Introduction

We are experiencing a new era in the governance of firms of all sizes - small as well as large. Boards of directors that earlier were considered to be passive, or just formal organizational bodies barely involved in strategy, and rubber-stamping decisions already been taken (i.e. Mace, 1971), have now received more attention among scholars and practitioners than never before (Monks and Minow, 2001). This wave of interest goes across national boundaries, and global medicines for developing and empowering boards have been prescribed. In the majority of cases are the introductions of "outside" directors the solution for developing boards.

The aim of this paper is to develop theory on boards and governance by studying the role and contribution of "outside" directors in small and medium sized enterprises (SMEs). Research and literature on SMEs have long recognized that "outside" directors can be beneficial for the growth and development of SMEs (Castaldi and Wortmann, 1984; Nash, 1988; Daily and Dalton, 1992). The bulk of empirical research on the role and contribution of "outside" directors has however mostly been conducted on large publicly held companies (c.f. Daily et al, 1998). There are consequently very few studies that have explored the role and contribution of "outside" directors in the context of SMEs, and those who do have often uncritically adapted concepts and theories developed for large corporations without adjusting the situation to differences in for example ownership involvement, and the general lack of internal resources that often characterize these ventures (Huse, 2000; Daily et al, 2002). There consequently seems to be deficiencies in our knowledge of the role and contribution of "outside" directors in SMEs.

The rest of the paper is structured as follows. The framework for analyzing our research question is developed in the next section. In this section we present various board role theories and their perspective on the contributions of "outside" directors. The section continues with the argument that SMEs is not a homogeneous concept, and that contingencies and contexts must be included in understanding these firms. In particular we present how family firms and ven-

ture capital-backed firms diverge. In the third section we illustrate our arguments by analyzing 52 research projects about the role and contribution of "outside" directors in SMEs. In the fourth section we present an analysis of the projects. The final section summarizes the conclusions and contributions of the paper.

"Outside" directors in SMEs – a literature review

Above we addressed the question of the role and contribution of "outside" directors in SMEs. Our research question will in this section be positioned in relation to existing board role theories and the use of the "outside" director concept in these theories.

Theories of board roles

Board roles can be categorized and listed in various ways. For the purpose of this paper we have focused on agency, resource based and resource dependence arguments in explaining the role and contribution of "outside" directors in SMEs. These theories have frequently been used to motivate for the development of boards (Johnson, Daily and Ellstrand, 1996). Other board role theories deal with property rights, the boards' institutional role, strategy role, disciplinary role, figurehead role, ethical role, auditing role, class hegemony role, etc (c.f. Hung, 1998; Zahra and Pearce, 1989).

Monitoring and independent directors – agency theory. It is often argued that privately held SMEs could benefit from the external oversight a governing board can offer by shielding the invested stakes of the key resource providers of the enterprise (equity holders, as well as debt holders and employees) from potential managerial self-interest, as well as from the risk that the CEO may mix personal and business goals (Castaldi and Wortmann, 1984; Nash, 1988; Hughes, 1996; Daily et al, 2002). This monitoring role of directors can be largely derived from agency theory (Fama and Jensen, 1983; Jensen and Meckling, 1976). The theory argues that the board can reduce agency costs and maximize shareholder value by being actively involved in the monitoring of managerial and firm performance (Fama and Jensen, 1983). From an agency theory perspective is the main contribution from "outside" board members their ability to introduce independent considerations prior to decision-making. The board of directors can in this perspective function as an important information system for external stakeholders to monitor managerial behavior and firm performance, and to reduce asymmetric information between contracting parties. The main contribution of "outside directors" according to agency theory is consequently their ability to be independent when over-see operating matters, protecting the assets of the firm, and holding managers accountable to the firm's various key stakeholders to ensure the future survival and success of the enterprise.

Advice and directors with expertise – resource theories (RBV). The resource-based view of the firm argues that a firm's internal environment, in terms of its resources and capabilities, is critical for creating sustainable competitive advantage (Prahalad and Hamel, 1990; Teece, Pisano and Shuen, 1997). Being aware of, improving, and protecting the unique resources of the firm will then reinforce firm strengths and rearrange firm weaknesses, and thereby improve a firm's competitive position. Small firms are however generally characterized by a lack of internal resources, and in-house knowledge may in many cases be scarce or non-existing (Storey, 1994). It has in this respect been considered important to have a board with experienced "outside" directors in order to overcome this internal lack of resources and complement the management with experience, knowledge and skills (e.g. Castaldi and Wortmann, 1984). The board of directors, and especially the "outside" directors, may hence be considered as a bundle of strategic resources to be used by and within the small firm as they can provide timely advice and counsel to the CEO and the management in areas where in-firm knowledge is limited or lacking. The resource-based view consequently recognize that can be a valuable source of competitive advantage through their professional and personal qualifications.

Legitimation, networking and co-opted directors – resource dependency theory. Resource dependency theory argues that the long-term survival and success of a firm is dependent on its abilities to link the firm with its external environment (Pfeffer and Salancik, 1978). A basic argument in the theory is that firms constantly must interact with its environment, either to purchase resources or to distribute its finished products. Firms should therefore seek to gain control over its environment to create more stable flows of resources and lessen the effects of environmental uncertainty (Pfeffer and Salancik, 1978). The "outside" board members are in this respect seen as a linking mechanism between the firm and its environment that may support the managers in the achievement of the various goals of the organization (Zahra and Pearce, 1989). The firm can also co-opt representatives from important external organizations as board members in order to achieve organizational goals (Pfeffer and Salancik, 1978:167; Borch and Huse, 1993). Hence, resource dependency theory recognizes that "outside" directors may add value to SMEs by helping to initiate and maintain control over critical

relationships, assets and contacts in the external environment of the firm.

Taken together, the theories indicate, both individually and combined, that the development of boards can be followed through the introduction of "outside" directors. However, the reason for recruiting "outside" directors, and the contribution of "outside" directors seem to vary across theories. Hence, various theories seem to have various rationales for explaining the role and contribution of "outside" directors in SMEs (Johnson, Daily and Ellstrand, 1996; Zahra and Pearce, 1989).

Understanding boards in the context of SMEs. In this study we want to explore boards and governance in SMEs. Mainstream research on boards and governance has however been focused on large Fortune 500 companies (Zahra and Pearce, 1989; Johnson, Daily and Ellstrand, 1996; Forbes and Milliken, 1999). Although these companies might give valuable insights into board practices and board behaviour do they represent only a minor form of economic organization. The major bulk of companies around the world are instead small firms that are involved in small-scale manufacturing and provision of services (Landström, Frank and Veciana, 1997). Focusing only on boards in large publicly held companies might thus limit our knowledge of the role and contribution of boards in other settings, for example start-ups, family businesses, or fast growing entrepreneurial ventures (Huse, 1998; Lynall, Golden and Hillman, 2003). This indicates that a relevant question is to which extent our current understanding and conceptualisations of "outside" directors can be used in SMEs without adjusting the situation to differences in context (Huse, 2000).

The question above is based on the assumption that expectations about boards may vary depending on the dynamics of board-stakeholder interactions (Huse, 1998; Huse and Rindova, 2001) and the relative power of various groups of internal and external stakeholders (Rosenstein, 1988; Gabrielsson and Huse, 2002; Huse, 2002). Such dynamics and power balances may vary depending on the context in which the firm operates. SMEs are in this respect often characterized either by ownership and control consolidated in one or a few individuals, or by close relationships between owners and managers (Storey, 1994). The context of SMEs may consequently vary from a context of large Fortune 500 companies, and various ownership configurations may also address questions about board compositional definitions as that of insiders vs. outsiders.

Two categories of SMEs that recently have received increased attention are family businesses (Corbetta and Tomaselli, 1996; Ward and Hardy, 1988) and venture capital-backed firms (Fried et al, 1998; Gabrielsson and Huse, 2002). In addition we also recognize other ownership configurations and contexts for SMEs, such as subsidiaries, joint ventures and partnerships (Kriger, 1988; Huse and Rindova, 2001; Goodall and Warner, 2002). These three groups firms will be described below.

Family businesses. Many SMEs are companies that are entirely owned by the members of a single family. These companies are generally considered family businesses (Corbetta and Tomaselli, 1996; Cowling and Westhead, 1996; Gersick et al, 1997). There are however many definitions of family businesses[1]. The broadest definition defines a family business as a firm where a family has the voting control of a company (e.g. Neubauer and Lank, 1998). This definition will include close to 95% of all registered companies in Europe (Mustakallio, 2002). In this paper we will use a common definition of a family business in order to highlight the special features of such firms: a firm where the CEO considers the firm to be a family business. This consideration means that everyday business life becomes as important as maintaining family traditions and building a future for generations to come.

Studies of boards in family businesses have found that they often have relatively few directors, with one or two family members on the board in addition to the owner-manager (Ward and Handy, 1988; Cromie, Stephenson and Monteith, 1995; Corbetta and Tomaselli, 1996). In the cases when there is an "outside" director on the board, it is often a person that has a close connection to the business, such as the family attorney, a banker or a friend of the CEO (Ward and Handy, 1988; Corbetta and Tomaselli, 1996). The board is moreover expected to have relatively little potential influence as the owner-manager often exercise power over the board through his or her central role in the selection and remuneration of directors, and by shaping the information provided to them (Ward and Handy, 1988; Johannisson and Huse, 2000). The typical board in family businesses can thus be pictured as a "rubber stamp-board" that only meets to formally approve what the owner-manager has already decided to do (Mace, 1971).

Literature on family businesses however point out that in firms where the second, or even later, generations has taken over ownership control over the company often differ significantly in their governance structures compared with first generation family businesses (Gersick et al,

[1] The definitions most often include one or more assumptions about family ownership, about the number of generations the firm has been in the possession of a family, and that the owning family also should have management positions.

1997). The complex ownership-situation that characterize many family businesses may hence create demands from distant (non-involved) family members on organized systems for control and influence among the various branches of a family – such as a board of directors (Neubauer and Lank, 1998).

Venture capital-backed SMEs. Venture capital backed SMEs are firms in which professional investors have invested alongside management due to the firm's potential for significant economic returns. Venture capital-backed SMEs are in this respect often found in emerging industries where new start-ups have the potential to develop into major economic contributors (Fried and Hisrich, 1995; Manigart and Sapienza, 2000). While family businesses by definition may be relatively old and mature firms, will venture capital-backed firms consequently often be young and fast-growing firms in which the need for alertness and proactiveness in turn calls for short-term planning and frequent follow-ups (Manigart and Sapienza, 2000).

Studies of boards in venture capital-backed SMEs have indicated that venture capitalists (VCs) often is a key stakeholder group that put pressure to change and develop boards in SMEs. Studies of venture capital backed companies for example reports that the boards are dominated by "outside" board members, with VC-appointed directors rather than management in control (Rosenstein, 1988; Rosenstein et al, 1993; Fried, Bruton and Hisrich, 1998; Gabrielsson and Huse, 2002). The VCs presence on the board of directors may for example help the firm's executives to focus their efforts to closely monitor firm performance and in developing systems to reward innovation and creativity (Fried et al, 1998; Markman et al, 2001). Moreover may VC appointed directors provide managerial competence and valuable resources through their experience and personal network built up during their careers, which can be of great help for young entrepreneurial firms (Deakins et al, 2000; Politis and Landström, 2002). The adoption of "outside" directors on the board is hence not only due to 'the power of purse', where the VC partnership wants to monitor CEO and firm performance, but is also a way for these small entrepreneurial ventures to get access to the expertise and networking resources that the VC possess (Rosenstein, 1988; Gabrielsson and Huse, 2002).

Other ownership configurations and contexts for SMEs. There are also various other featured ownership structures in SMEs than the typical family firm or venture capital-backed firm. Subsidiaries are one common example (Kriger, 1988; Huse and Rindova, 2001). The management in the parent company often constitutes the board in subsidiaries, and the parent company management is sometimes supplemented with employee directors, and even some "outside" directors (Björkman, 1994). Joint ventures, partnerships and employee-owned firms are other ownership configurations in SMEs. Firms with such ownership structures may have particularly active boards, but the board members are most often the partners and both of these examples have distinctive governance mechanisms and practices (Gulati and Westphal, 1999; Goodall and Warner, 2002).

Framework for the analysis

Through the literature review we have developed a framework for analyzing the role and contribution of "outside" directors, and the "outside" director concept in SMEs. The literature review above indicates the importance of using multiple theories for understanding this issue. Moreover, the review indicates that various ownership configurations and contexts seem to be a main criterion for understanding alternative logics for having "outside" directors in SMEs. This gives us a framework with two dimensions: i) board role theories and ii) ownership configuration and context. The framework suggests that various theories (agency theory, resource based theories and resource dependence theory) can be applied to different kinds of SMEs (e.g. family businesses and venture capital-backed firms) through expectations about the role (monitoring, providing advice and council, and managing resource dependencies) and characteristics (independence, expertise, boundary spanner) of "outside" directors. This framework will now be used to explore the role and contribution of "outside" directors in a sample of studies of boards in SMEs.

Illustrative sample

In this section we will present the illustrative sample and main concepts used in the present study. We decided to use a review of 100 student reports on boards of directors to meet our research question of the role and contribution of "outside" directors in SMEs. The student reports are all empirical studies of boards in Norway and Sweden. For the purpose of this paper we selected reports that included issues relating to "outside" board members in SMEs. A total of 52 reports met these criteria. A more general overview of the accumulation of knowledge from these 100 reports is given in Huse and Gabrielsson (2002).

The sample: 52 research reports

The empirical data used in this paper consists of 52 unpublished empirical research reports, in

which Norwegian and Swedish master students have collected data on boards of directors between 1989 and 2000. A variety of methods were employed in the research reports, from one-firm case studies till large-scale postal questionnaire surveys. In some cases even studies of board minutes and participant observation were employed. An overview of how the 52 studies fit into the framework developed in the previous section is presented in table 1 below.

Table 1. The reports: theories and types of firms

Board role theory	Agency theory	RBV	RDT
Board role	Control/ monitoring	Resource: Advise and council	Managing dependencies: Source for co-optation
"Outsider" characteristics	Independent	Expert	Boundary spanner
1. Family businesses	5 projects	11 projects	2 projects
2. Venture capital backed firms	5 projects	4 projects	3 projects
3. Other SMEs (Subsidiaries, joint ventures, employee-owned firms, firms with dispersed ownership)	7 projects	8 projects	7 projects

The table shows how the various reports match the framework developed in the literature review. The theoretical perspectives used (agency theory, resource based theory and resource dependence theory) and the types of firm in focus ("family business", "venture capital-backed firms", or "other kinds of firms") are displayed. In the group of "other kinds of firms" we find studies of subsidiaries, joint ventures, employee-owned firms and small firms with dispersed ownership.

Main concepts

The main concepts in this paper are "outside" directors, small and medium sized enterprises (SMEs), family businesses, and venture capital backed firms. Definitions of family businesses and venture capital backed firms has been presented and discussed in previous sections. We will here present how we will use the concepts "outside" directors and small and medium sized enterprises (SMEs).

"Outside" directors. "Outside" directors in SMEs often include directors who are neither employed as managers, nor are family members (or relatives) to the CEO. Earlier studies have however reported the many ways to define insider/outsider ratios (Johnson, Daily and Ellstrand, 1996). Our research question implies to show how such definitions are theory- and context- based. More specifically, we ask question about who are "outsiders" of boards in SMEs.

Small and medium sized enterprises (SMEs). The main definitional difference between large corporations and SMEs is company size, but size can be measured according to sales, number of employees, equity, market prices, market shares, etc (Storey, 1994). In this paper we will not make any clear definition of SME size other than that SMEs are different from large publicly held corporations, such as less structurally complex and less formalized, have limited capital and manpower, and are managed directly by their owners (or part-owners) in a "personalized" way (d'Amboise and Muldowney, 1988; Storey, 1994).

Analysis and results

The literature review presented a framework for analyzing the role and contribution of "outside" directors. The framework used the theoretically derived board roles and firm category as sorting variables. We used the definition of an "outside" director as a mediating variable. The analysis was then conducted by investing how the generally accepted concept of an "outside" director was influenced by theory and context in the various empirical reports. A summary of the findings is showed in table 2 below.

The role and contribution of "outside directors"

Family businesses. The "outside" directors in family businesses had various contributions, depending on the theoretical approach taken. The descriptions of the "outsider" directors also varied. In the reports using the agency theory perspective was the contribution of the "outside" directors mainly described as reducing information asymmetry between various branches of the family, or between the family and important external stakeholders. Reports using the resource-based perspective highlighted the role of "outside" directors in bringing resources and competencies into the firm, and bringing a detached view on the family business, involving key stakeholder interests and public responsibilities. Also, especially in more mature family businesses, the possibility to avoid the risk of "in

breeding" (Johannisson and Huse, 2000) was much valued. The role of "outside" directors from a resource dependence perspective was linking the firm to its external environment by networking activities. This was particularly the case in periods of expansion. Moreover, during CEO successions the "outside" director helped the family business with signaling legitimacy and stability in relation to external stakeholders.

Table 2. "Outside" Directors and Their Contribution on Boards in SMEs

	Agency theory - control	RBV – advice and counsel	RDT – managing resource dependencies
Family businesses Outsiders' contribution	Reducing information asymmetry among branches of the family, or for external stakeholders.	Bringing resources and competencies into the firm. Reducing the risk of in-breed and bringing a detached view on the family business.	Helping with contacts and networks during expansion (e.g. during internationalization). Legitimation during CEO successions.
Who is an "outsider"?	Experienced non-family person on whom the family and external powerful stakeholder trusts (often the family lawyer).	Experienced non-family person on whom the CEO/dominating family members trust (family friend, family lawyer, accountant or consultant).	Experienced non-family person on whom the CEO/dominating family members and other powerful stakeholders trust.
Venture capital backed firm Outsiders' contribution	Monitoring managerial and firm performance to maximize economic returns for equity holders (VC's and/or entrepreneurs').	Complementing entrepreneurs' lack of competence in key functional areas, such as finance, marketing, etc.	Using their network to recruit key personnel and to attract additional funding.
Who is an "outsider"?	VC, VC appointed director, or other director on whom the VC trusts.	VC, VC appointed director, or other director on whom the VC trusts.	VC, VC appointed director, or other director on whom the VC trusts.
Other SMEs Outsiders' contribution	Reducing information asymmetry and protecting shareholders against managerial indiscretion.	Strengthening the resources and capabilities of the firm.	Offering legitimacy in the business community, and influencing important stakeholder groups.
Who is an "outsider"?	A non-executive shareholder, or businessperson not employed by the firm on whom shareholders trust.	Experienced businessperson on whom CEO trust, often an executive in another firm.	High profiled person on whom external stakeholders trust.

The empirical reports moreover showed that executives and CEOs in family businesses seem not to outright avoid "outside" directors, but they do not necessarily always welcome them either (e.g. Johannisson and Huse, 2000). Suspicion and family politics are common ingredients in the selection process, and the choice is not always in favor of the "outsider". Noteworthy is that mature family businesses (firms in the 2nd or 3rd generation) were more likely to employ "outside" directors, either to monitor firm performance for the firm's main stakeholders (i.e. various branches of the family or the bank), or as a sounding board for aging CEOs (e.g. Fiegener, et al, 2000).

Then who are the "outside" directors in family businesses? The reports show that this varied somewhat depending on the theoretical approach applied. In studies using the agency theory perspective was the "outside" director a person on whom the family trusts could be independent from the influence of the management team. This could for example be the family lawyer. From a resource based perspective was the "outside" director an experienced person on whom the CEO and the dominating family members trust. This could be a long time family friend, the family lawyer or other persons the family has known for a long time. From a resource dependence theory are "outside" directors supposed to be boundary spanners, and in the family firms they are experienced persons that the CEOs, family members and other powerful stakeholders trust. All theoretical perspectives consequently highlight *experience* and *trust* as two main features for understanding the role and contribution of "outside directors" in the family business context.

Venture capital-backed firms. The contribution and definition of "outside" directors in venture capital backed firms differ somewhat from that of the family business. Reports using the agency theory approach highlighted the "outside" directors' contribution in reducing managerial

opportunism, and monitoring managerial and firm performance to maximize economic returns. Reports using the resource-based perspective the "outside" directors highlighted that "outside" directors' complemented the lack of in-house competence. The "outside" directors' were for example often complementing the management's lack of competence in various functional areas such as finance, general management, marketing etc. From a resource dependence perspective the "outside" directors contributed with establishing and maintaining important links to external stakeholders. The "outside" directors' were in this respect mainly active in using their networks to find and recruit key personnel, and in receiving additional funding during its various stages of development (Rosenstein, 1988). From the CEOs point of view, the board was hence a much-valued resource despite the strong monitoring focus.

The "outside" directors in the venture capital-backed firms were the VCs, or a person appointed by the VCs in all three theoretical perspectives. It happened that the entrepreneur had appointed other "outside" directors to counterbalance the influence of the venture capitalist, but then it was a person that also was trusted by the venture capitalists. A main difference from family businesses is hence that while family businesses recruit directors on whom family members trust do venture capital-backed firms recruit directors on whom the VCs trust.

Other SMEs. In addition to family businesses and venture capital backed firms did the research reports include samples from subsidiaries, employee-owned firms, partnerships, joint ventures etc. Reports using the agency theory perspective in these kinds of firms indicated that "outside" directors were recruited primarily to check against managerial indiscretion and reduce the information gap between external owners and the management team (which sometimes was part-owners). This was the case both when there was a single owner (such as a parent-company) or when the ownership was dispersed among several owners outside the firm. Reports using the resource-based perspective highlighted the "outside" directors' role in strengthening the resources and capabilities of the firm by contributing with their expertise and experience. Reports using resource dependency theory described "outside" directors as helpful in offering legitimacy in the business community, influencing stakeholder groups, and seeking to achieve competitive advantage through networking activities. Both the resource-based and the resource dependency perspective indicated that "outside" directors could be regarded as much valuable resources that could be exploited for a rather low cost, as they brought valuable expertise, and access to valuable resources by making their business and personal networks available to the small firm (Borch and Huse, 1993).

The definition of an "outside" director in this group of SMEs also varied depending on the theoretical perspective applied. In reports using agency theory, "outside" directors were most often external owners seeking influence over company decisions. In reports using resource-based perspective was "outside" directors experienced businesspersons on whom the CEO trusts - often acquaintances that were CEOs in other firms. The resource dependency perspective described "outside" directors as high profiled persons on whom external stakeholders trust, that were chosen for his or her reputation.

The above illustration shows how "outside" directors can play multiple roles in SMEs. Moreover, the concept "outside" director is not the same in different theories and in different empirical settings. This leads us to question previous universalistic approaches and general theorizing when trying to understand the role and contribution of "outside directors across various types of SMEs. From an agency theory perspective is the most important qualification for "outside directors their ability to be independent (Fama and Jensen, 1983). But should independence be defined in relation to the firm, the management, or the owner-family? In family businesses "outside" directors are often defined as non-family directors. The reports however show that "outside" directors in family businesses tend to have strong ties to the CEO and/or the dominating family members. Their independence can therefore be questioned. It can even be likely that non-executive members of the family may be more independent than an "outside" director that is recruited through the professional and private network of the CEO. In venture capital backed firms, "outside" directors were often defined as VC or VC appointed directors, i.e. directors independent of the entrepreneur, despite that VCs also can deliberately withhold information, not perform as agreed, and pursue short term self interest seeking behavior to the expense of other stakeholders. In the third category of firms (other SMEs), "outside" director was often a non-management shareholder. These findings clearly indicate that research on director independence in SMEs must include explicit discussions of what directors are supposed to be independent of.

Moreover, both the resource-based view stressed other "outside" director qualifications than independence. In the resource-based view "outside" directors were supposed to have a good knowledge of the market and the industry in which the firm operates, so that their experience could improve firm performance. Resource dependency theory on the other hand stressed that

"outside" directors had a well-developed personal and business network that could mediate trust, reduce internal resource dependencies, and establishing links between internal and external stakeholders. The various theoretically derived expectations on the role and contribution of "outside" director make it hard to include all these qualifications in the same person. Alternative operationalizations of "outside" directors' independence and expertise should be sought depending on theory and context.

Taken together, the analysis indicates that "outside" directors can be critical for effective boardroom governance in SMEs, but also that the traditional definition of an "outside" director as a non-management director is an overly simplistic term (Daily, Dalton and Johnson, 1999). Our understanding of the role and contribution of "outside" directors in SMEs seem instead to vary depending on the theoretical framework used, and the type of firm being studied. The concept of an "outside" director is not generic and should not be used interchangeably without reflections of what the consequences will be. Hence, an open and context based definition may be required to understand the various roles and contributions of "outsider" directors in various settings of SMEs.

Summary and conclusion

The aim of this paper has been to develop theory on boards and governance by investigating the role and contribution of "outside" directors in SMEs. Various board roles theories have been presented, and so also theoretically derived definitions of "outside" directors. Based on an analytical framework of board role theories and different firm categories, we have analyzed the role and contribution of "outside" directors through a review of research reports on boards in SMEs. Firms are shown to recruit "outside" directors in order to develop their boards for various reasons. The illustrative sample shows that the widely used concept "outside director" is not the same in different theories and in different settings. A main contribution of this paper is raising the consciousness about how "outsider" definitions in practice vary across theories and contexts. The empirical observations about "outside" directors is largely dependent on the theoretical lens used to understand their role and contribution, and a high degree of consciousness should be displayed when moving the "outside" director concept from one context to another.

In this paper we have contrasted various board role theories against different types of ownership structures in SMEs to understand the role and contribution of "outside" directors in this setting. However, the context for SMEs goes beyond ownership structure. A life cycle approach is for example often considered as important to understand boards of directors in SMEs (Huse, 1998; Lynall, Golden and Hillman, 2003), and so are other contingencies such as industry, firm complexity, and the presence and role of the founder (Randøy and Goel, 2002; Gabrielsson, 2003). These things are however largely unexplored issues, and it is consequently highly relevant for future research on boards and governance to continue to investigate how various contingencies in and around SMEs could influence the development of boards and the role and contribution of "outside" directors. These insights would then be significant contributions to our knowledge of corporate organization and governance in SMEs.

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