HARCOURT BOARDROOM RESOURCES

BOARD COMMITTEES – HOW MANY AND WHICH ONES?

Boards have packed agendas and limited time. The list of mandatory items seems to be getting longer each year, the number of short-term topics for consideration higher, and the time available for discussion and long-term planning shorter. Directors are frustrated and complain that they are not discharging their duty properly. What can be done?

One way to ease the burden of the board itself is to refer specific matters to committees for a more detailed discussion. This is both convenient and efficient, and should be encouraged. But how far should the board go, and for what matters?

In most jurisdictions, corporate law mandates at least an audit committee and, generally, a remuneration committee, and sets out the required composition of these committees (both number and, more importantly, independence of members). For example, in the banking sectors, four committees are now required in most countries: audit, risk, nomination, remuneration.

Beyond the minimum requirements, companies can do what they want. Here are some of the considerations they might want to take into account when discussing whether to set up board committees:

1. "Deep dives": Committees are about taking "deep dives" into certain matters. Board members should be satisfied to delegate to some of their colleagues, and particularly the committee chair, the detailed examination of these matters. The role of the committee is not to decide in lieu of the board, but to prepare the board's decision, set out the assumptions and clarify the issues.

2. Technical and complex: As a result, matters to be delegated to committees are generally technical and complex in nature – accounts, large capital expenditures, ethics & compliances issues, remuneration plans, governance charters, etc. These matters require very lengthy examinations of facts, assumptions and options. The committee report to the board should set out these elements clearly, and can include a recommendation, in order to enable the board to decide. Boards are more hesitant to delegate more general questions of strategy, business oversight, budget approvals or board appointments.

3. Standing and "ad hoc": A board may set up "standing" (i.e. permanent) or "ad hoc" committees. The latter are, by definition, limited in time and focused on a narrower set of issues. "Ad hoc" committees are often set up in response to a crisis situation – monitoring of an investigation, crisis management, etc. They may also be interpreted by management as a sign that the board does not trust them. Hence the need to get management's buy-in. In all cases, they should be handled with parcimony, specific start and end dates, and clear agendas.

4. Priorities: A board may also feel that a committee (either standing or "ad hoc") is necessary to send out, internally and externally, the message that it considers a particular matter to be a priority, and that is will get involved in closely monitoring it. This has been one of the reasons for the proliferation of committees after the financial crisis, particularly in the banking sector – but there, too many committees have had the opposite effect of blurring priorities.

Apart from the audit and the remuneration committees, here are some of the board committees that appear quite regularly:

1. Governance and nomination: These matters are often bundled with remuneration into a committee that deals with all "people" matters. It should be noted that in certain jurisdictions (Scandinavia in particular), nominations to the board are a completely separate process, and not in the hands of the board itself.

2. Risk: The oversight of risk is generally the remit of the audit committee. There is nothing wrong with this practice, as long as the committee manages its work plan properly. Unfortunately, too many audit committees consider that their real responsibility is to deal with the accounts, and that they will deal with risk if and when they have time – which turns out to be not often enough. Whilst an audit and risk committee is perfectly adequate for many sectors, there are sectors where a separate risk committee should be given consideration (capital intensive sectors, sectors where the production process is inherently risky, etc.), and some (e.g. the banking sector) where it is mandatory in most jurisdiction.

3. Strategy: It is unusual for a well-functioning board to set up a strategy committee. Strategy is at the heart of what a board is about, and not many directors are ready to delegate the strategy discussion to a sub-set of the board, or to decide on a strategy without being involved themselves in a thorough discussion. If the committee report gives rise to a whole new discussion at board level, maybe the discussion should never have left the board in the first place. And if the strategy committee's recommendation is accepted without a full discussion, it is unclear that the board is doing its job properly. The reality is that a strategy committee will be in place where the normal functioning of the board is impaired – too many members, existence of conflicts of interest, employee representatives, leaks at board level, etc. Rather than set up a strategy committee, the board would do well to reflect on why it think a separate committee is necessary.

4. Executive/management: boards are about oversight and strategy, not about execution. So a board "executive committee" is an oxymoron. However, the practice in some jurisdictions is to have such a committee. Its role is generally to oversee the business more closely and more regularly than the board is willing to do – in other words, it is really a "mini-board". However well it is run, a board "executive committee" necessarily blurs the lines between the board's role and the management's role. Its presence is characteristic of a "two-tier" board: an "executive committee" where the directors are involved and spend the time required, and the rest of the board where the directors make token appearances. Every trend in modern corporate governance goes against that type of board and board practice.

5. Bid/tender: In certain industries, large tenders have to be approved by the board. It is normal in these situations to have special committee review the details of the tender, the business plan underlying the response, and the report to the board with a recommendation. Certain companies have a financial commitment committee (sometimes bundled with the audit committee), which serves the same purpose.

6. Ethics & Compliance: More and more companies set up a specific committee to deal with issues of ethics and compliance. In practice, this committee end up overseeing all issues relating to the corporate reputation and "license to operate" – an open-

ended agenda, intricately linked to the underlying business. A more limited step in that direction is a CSR committee.

The list of committees can be very long indeed, as boards constantly come up with reasons to set up new committees. Most boards limit their committees to 3 to 5. However, committees will serve their purpose only if they correspond to a need, recognized by board and management, and the committee meetings are handled properly. See "Making the Most of a Committee" – Harcourt IGN, February 2016.

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