Excos and the balance of power

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The Exco may be the most powerful committee on the board, but is it at risk of being a "board within a board" and increasingly less relevant?

Of the several board committees within a company, the executive committee, or Exco, stands out, both for its influence as well as the conspicuous absence of guidelines regarding its governance.

The Exco is often made up of the more active members of the board. It is usually chaired by the board chairman, and its influence and powers are seen as above that of the other board committees.

While the Code of Corporate Governance encourages the formation of, and provides guidance on the audit, remuneration, nominating and board risk committees, there is no mention of the Exco.

The characteristics, powers and functions of Excos, as well as some of the leading practices concerning the establishment of Excos, are thus worth revisiting in the current circumstances.

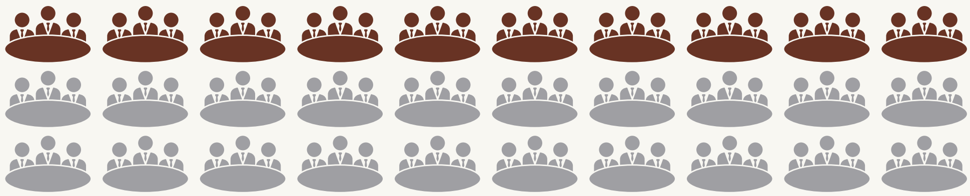
The Profile of an Exco

A review of the top 30 companies in the STI provides a profile of what Excos can be like (see box titled "Exco Profile").

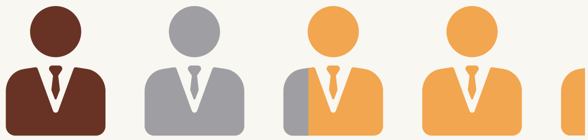
Profile of Excos

The following profile of Excos is obtained by a survey of the Straits Times Index's (STI) 30 constituents.

1. Number of boards with Excos: 1/3 (10 out of 30)



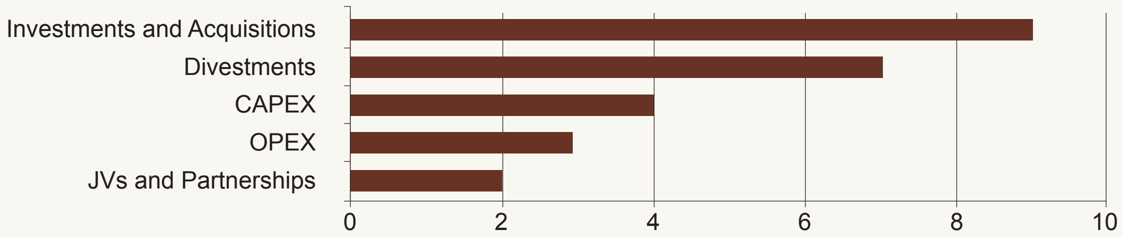
2. Exco composition: 4.4 directors with 1 ED, 1.2 NI-NEDs, and 2.2 IDs.



3. Number of meetings per year: 5.3 compared with 5.9 for full board meetings.

4. The Exco's authority

Exco's Approval Authority for Transactions



5. Non-approval Exco functions

Other Exco Functions

As can be seen, one third of the companies have Excos. This ties in with the broader 2015 SID-SGX Board of Directors Survey which also shows that one third of listed boards have Excos.

The Exco's composition tends to be relatively similar across companies. It would be chaired by the board chairman, and its members comprise executive directors (who have greater availability given their full-time commitment to the company) and senior members of the board (such as the chairmen of board committees).

The powers and responsibilities of Excos can vary considerably. This state of affairs reflects the diversity and complexity of needs that boards face.

While 10 per cent of the Excos were not specifically assigned approval authority, most were, with 70 per cent disclosing the existence of a monetary limit on their approval authority.

The most common form of authority delegated to Excos was approval of investments and acquisitions, closely followed by approval of divestments. Notably, a further six of the 20 STI constituents that did not have Excos had established Investment Committees, presumably for that purpose.

Excos are usually also tasked with (non-approval) functions, ranging from review of budgets, plans and strategy to guiding management on execution.

Performance Value

From the chart, it would appear that the Exco's substantive contribution is in the area of strategy and its implementation. In reviewing documents and corresponding closely with management, Excos can monitor management's progress, on implementing strategy, at a greater depth than the board would be able to, given the constraints on the board's time and attention.

Both the board and management can benefit from the Exco's support under this arrangement. Management can sound the Exco out on proposals to get a sensing of how the full board would receive them, and potentially refine them to cater to the board's likely concerns and information needs.

If the strategy set by the board is not working, regardless of the cause, the board is likely to pick up warning signals earlier through the Exco's monitoring and reporting. This gives the board more time to consider if a change in strategic direction is needed, which could be of particular importance when an organisation is dealing with competition fueled by disruptive innovation.

Club of the Select

In recent times, Excos have been criticised as being a "club of the select" or "board within a board", with the spotlight being cast on incidents where Excos de facto replaced the board as their organisation's apex decision-making body.

The fact is that the ability of the directors not on the Exco to contribute varies from one organisation to another. Where the Exco reports to the Board in a timely manner, and shares a common understanding of the risk-reward tradeoffs the board as a whole is prepared to accept in pursuit of strategic objectives, the directors not on the Exco are more likely to remain just as effective. On its part, the Exco should also refer decisions to the full board where it envisages that the excluded directors are likely to take an opposing view.

The real risk lies where the Exco conducts its proceedings in a manner that is less than transparent, or wields excessive authority, thereby relegating the board to a "rubber-stamping" role. In such a situation, the full board is notified of Exco decisions after the fact, and the directors not on the Exco lack the means to meaningfully alter or reverse any of the Exco's decisions.

InfoComm Impact on Excos

Even with a sound system of checks and balances, there remains a question as to whether Excos can continue to be relevant in today's digital age.

Since one third of boards have Excos, that should, perhaps, be an *ipso facto* indication of their value. That said, there are companies that are discontinuing with their Excos.

Given how connected modern communications are, many of the practical challenges boards once faced in being informed and consulted have largely gone away. The Internet, personal computers and mobile devices keep directors connected wherever in the world they may be. Virtual attendances at board meetings are widely accepted. Board portals and cloud storage enable directors to retrieve electronic documents and interactively mark up at the tap of a screen. Dashboards that track performance measures, such as risk indicators on a live basis, are increasingly becoming commonplace.

With technology used so pervasively to conduct board affairs, directors are now in a position to be more involved in the affairs of a company than ever before. In fact, many traditional Exco functions are being made redundant. Although some functions such as evaluating major transactions and crisis management are best done by a small and focused group of directors, it is becoming increasingly clear that they can also be done by special purpose ad-hoc board committees that are set up for those purposes, rather than by a standing committee such as the Exco.

Finding the Right Balance

How then to make use of the Exco for its benefits while avoiding its disadvantages?

One way would be to use the Exco primarily for alleviating the board's workload in terms of performance monitoring and coaching to management on strategic implementation. This is akin to a Strategy Committee.

The Exco's approval authority, where granted, should be set at a reasonably low limit—a step up from management with major transactions still going to the board.

Minutes of Exco meetings should be circulated to the full board on a timely basis, and should adequately explain the grounds of the Exco's decisions for the benefit of the directors not on the Exco.

Notably, directors cannot abdicate responsibility for the performance aspect of governance by delegation to the Exco. Rather, the establishment of an Exco should complement directors' continual responsibility to stay informed of corporate affairs, and the board's other initiatives in the area of strategy—such as board strategy retreats, strategic deep dives on the board agenda, etc.

Given the availability of empowering technology, and balanced against the risk of an over-concentration of power in the Exco, many companies have chosen not to have an Exco or discontinue with having an Exco.

Yet, some companies, especially those with more complex organisational structures see a real need for the Exco. Each company therefore needs to find its own sustainable set of checks and balances to put in place. The key fundamentals of transparency, diversity and inclusion that should be part of every company's drive towards greater performance and accountability remain the same regardless of the existence or absence of an Exco. ■

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