FINANCE COMMITTEE, FINANCIAL DECISIONS, AND FIRM PERFORMANCE

Jane Q. Xie, St. Edward's University, Austin, Texas, U.S.A.
Matthew J. Behrend, St. Edward's University, Austin, Texas, U.S.A.
Joseph Nketia, St. Edward's University, Austin, Texas, U.S.A.

dx.doi.org/10.18374/JIFE-21-2.3

ABSTRACT

This paper studies whether a stand-alone finance committee is beneficial to shareholders and which finance committee characteristics play a key role. Using a sample of the Standard and Poor's 500 companies, we find that simply establishing a finance committee may not be beneficial. However, in firms with an established finance committee, firm performance improves if the chair of the finance committee is independent and the number of the chair's active board memberships is limited to three or fewer. The number of committee memberships the chair has in the same company does not negatively affect firm performance. The finance committee chair simultaneously serving on an audit committee does not significantly improve firm performance. Finally, finance committee size does not play a role in firm performance and finance decisions.

Keywords: *Finance Committee, Board Committees, Firm Performance, Financial Decisions*

1. INTRODUCTION

The board of directors has two main responsibilities: advisory and oversight. To better serve shareholders, firms form various board committees that perform oversight functions and monitor the specific activities of the firm and management. The ultimate goal of the various committees is to improve firm performance and create value for shareholders. All boards of publicly traded companies in the United States are required by the Sarbanes-Oxley Act and stock exchange regulations to establish three standing committees: audit, compensation, and nominating/governing committees. Some companies have voluntarily formed specialized board committees such as finance, executive, risk, science and technology, strategic planning, corporate social responsibility related, etc., of which the most popular and prevalent is the finance committee.

One major reason for the increasing popularity of finance committees is that "*audit committees are overburdened by their increased obligations to oversee the details of the reporting and compliance processes. As a result, the audit committee no longer has enough time to seriously consider broader financial topics. If directors are going to have meaningful input into the broad financial issues faced by any public company, they need to form a finance committee with the time and expertise to address the issues."* (https://www.cfo.com/governance/2017/05/create-finance-committee-every-public-company/) In addition, firms with complex business models tend to have a large board, which is more likely to establish specialized committees such as a finance committee to mitigate costs and effectively perform monitoring roles (Boone, Field, Karpoff, & Raheja, 2007; Coles et al., 2008; Linck, Netter, & Yang, 2008). Having multiple specialized board committees may maximize the contributions and talents from board members and improve corporate governance (Spira and Bender, 2004).

The role of the finance committee is broad. For example, the finance committee of 3M states that it "assists the Board with its oversight of the Company's financial structure, including its overall capital structure, sources and uses of funds and related cash and financing plans, the Company's financial condition and capital strategy, and financial risk management." The responsibilities and roles also include monitoring, reviewing and evaluating dividends, stock repurchases, short- and long-term borrowings, mergers and acquisitions, capital allocation, funding and liquidity strategies, etc.