

# Risk Management Committee Attributes: A Review of the Literature and Future Directions

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**Abstract** The aim of this paper is to review existing literature related to the risk management committee attributes (RMC) that can facilitate transactions between board committees and add value to corporations. The emphasis of this study is on RMC as it has become a crucial element, especially after the collapse of large corporations. RMCs have attracted the attention of academics and become one of the important factors that enhance the companies' performance as well as the quality of financial reporting (FRQ), and its demographic attributes are expected to play an important role in corporations. However, prior studies on the area have found inconclusive results and provide several gaps in the literature due to the mixed findings. In addition, prior studies highlight the RMCs attributes that affect corporate's performance and also the reporting quality and provide an urge to conduct more researches in related fields. Taking the period from 2003 to 2021, this paper reviews previous studies and gives a better understanding of RMC's role and future research directions. In addition, this study provides recommendations to the policymakers, regarding the demographic attributes of RMCs that can influence corporate performance and its FRQ. Finally, this review demonstrates that businesses should concentrate on these mechanisms to strengthen their performance and their reporting quality.

**Keywords** Risk Management Committee Attributes, Financial Reporting Quality, Board Committees, Corporate Financial Performance

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## 1. Introduction

Risk Management Committee (RMC) has become one of the crucial players in the current corporations' era. Being part of the board of directors, this sub-committee is expected to provide adequate resources to the board and assist the company in monitoring the management's activities which enhance the performance of firms and minimize the propensity of earnings manipulations (EM) [1]. According to a study done by [2], RMC pursues a vital role in reducing the operational risks and enhancing performance by ensuring that the management avoids risky projects and invests in profitable ones. In the same vein, according to [3] "establishing a standalone RMC can enhance the effectiveness of the risk-assessment process, and in parallel to that, reduce financial risks (e.g., financial crime prevention)".

In other words, RMCs play pivotal roles for the firms' success or failure. However, in most countries around the world, risk supervision traditionally has been one of the responsibilities of the audit committee and board of directors, which has resulted in some confusion. According to [4], the audit committee in such a situation will be given more responsibilities because the risks related to operations are diverse and broad, including "both financial and non-financial risks", which is not under the control of the audit-committee. Previous researches by Yatim [5], Brown,

et al. [6], and Kallamu [7] have backed up this claim, concluding that in today's dynamic and high-risk corporate environment, ACs are not sufficient for monitoring the financial and non-financial risks. Furthermore, the AC's dual role, its complex functions, the expanded responsibilities, and the lack of resources such as expertise and time required to monitor the organizational risks, have highlighted the need for the formation of separate RMCs.

RMCs have been identified as key factors that influence a corporations' success according to several studies. The attributes of the RMC are likely to have a major effect on a corporate's performance [8, 9]. This paper focuses on RMC attributes since it has become an important component of the hierarchy of management. Thus, the current review sheds light on RMC's attributes and their impacts on businesses. It is therefore important that this review helps and guides researchers to better understand the roles and functions of RMCs in businesses. The organization of this paper will be as follows: the first section provides a review of previous researches on RMC attributes. The second section contains crucial information regarding the demographic attributes of RMCs and their influence on corporate performance. The third section looks at the existence of RMC and its influence on FRQ. The methodology is seen in the fourth section and at the end of this review, the discussion and conclusion are presented.

## 2. Literature Review

### Risk Management Committee Studies:

The theory of corporate risk management was previously presented by Stulz [10], who claims that the major purpose of risk-management oversight is to protect the corporations from potential costly situations that may potentially cause financial distress. To look at it another way, risk management oversight was created and designed to mitigate the potential costs of dealing with financial challenges while maximizing and exploiting competitive advantages. Alles, et al. [11] posit under the agency theory that a separated RMC is expected to strengthen the organization board monitoring and deter managers from engaging in non-ethical practices. Likewise, according to the resources dependency theory, the RMC as a board sub-committee is expected to provide additional resources and skills to minimize the possible agency problems and improving the reporting earnings [12].

There has been an increase in the researches on risk management topics as seen in the last decade. Arévalo [13] claimed that corporations should introduce a mechanism to control financial risks so that these corporations do not experience excessive indebtedness correlated to economic growth. Prior studies have found that the RMCs influence the decision-making process. For instance, Subramaniam,

et al. [1] studied the stand-alone RMCs', the governance practice, and financial reporting quality; Ng, et al. [4] studied the RMC role in firms' underwritten risk that has a relationship with the going concern. Abdullah, et al. [14] studied the RMC and hedging activities as well as the information disclosure. Wu, et al. [15] show that the RMC of listed companies in Malaysia influences the efficiency level of the firms. Terjesen, et al. [16] claimed that the burden of risk oversight has been carried out by the AC. Therefore, the presence of an RMC is anticipated to influence the role of risk oversight functions positively which will result in improving the corporate' performance and market value. Kallamu [7] studied the risk management committee and the market valuation and accounting return. Jia [17] studied the effects of RMC diversity gender on a corporate's probability of having financial distress.

Several RMC attributes have been identified in the previous researches, such as separate RMC, size, meetings, independence, expertise, and overlap, that impact different firms' results. In addition, the RMCs have been identified as committees that have a substantial degree of control over the quality of reporting. Previous empirical studies have confirmed these allegations [7, 18]. Recently, Bhuiyan, et al. [19] using Australian firms from 2001 through 2013, studied the relationship between separate RMC in a corporation and the quality of financial reporting. Their study found that the presence of an RMC is more likely to reduce the discretionary accruals; which indicates that the quality of earnings information improves when RMCs are in operation. The study has also indicated that the RMC existence increases the company's audit fees. Taken together, this river of research highlights how the RMCs influence the corporations and provide motivation for conducting further researches in related area.

### 2.1. Risk Management Committee and Corporate Financial Performance

Corporate performance is one of the primary considerations that are used to attract the investors' attention to a business. The financial performance of the company is often used to measure the management's policies effectiveness of the management's activities and its information is also used by the stakeholders in the financial reporting circle to make several economic decisions [20]. By concentrating on significant risks, challenging risk management assumptions, and guiding the board on levels of the risk appetite & tolerance, the risk management committee ensures that risk oversight is aligned with the organization's strategy [21]. Boards of directors need to create a formalized risk management system within organizations, as a more recent development, that would complement the board of directors' oversight responsibilities [22].

### 2.1.1. The RMC Independence and Corporate Financial Performance

The independent RMC members are expected to secure all the necessary information and withstand any pressure from managers to control the company risk which will result in enhancing firm performance [23]. Many codes of corporate governance around the world require firms to constitute their RMCs with a majority of independent directors to carry out their functions independently. This agrees with the agency theory proposition that outside directors can monitor and detect any personal-gain actions by management and reduce the agency costs. Kallamu [7] used data of Malaysian listed-firms for a period of five years and questions “whether RMC attributes have an impact on corporate performance measured by ROA and Tobin’s Q”. His findings indicate that the existence of RMCs that have majority of independent non-executive members has a significant positive impact on corporate performance and market valuation. Another study done by Wu, et al. [15] examined the effects of RMC characteristics including independence on corporate efficiency using data consist of 34 insurance companies, the study findings suggest that the proportion of independent members in the RMCs has significantly and positively affected the efficiency of firms. Similarly, Kantudu and Samaila [24] examine the effect of corporate governance characteristics on FRQ (measured by EM) by using a sample of Nigerian oil firms. The study finds that independent directors can reduce the occurrence of earnings manipulations practices.

### 2.1.2. The RMC Diligence and Corporate Financial Performance

In accordance with resource dependence theory, frequent board meetings bring outside resources, through which, during the meeting discussion, the directors bring their expertise and knowledge as important resources, which contribute to efficient decision-making. Zaman, et al. [25] argue that the Frequency of meetings is linked to higher effectiveness while a lower frequency of meetings indicates lower effectiveness. Besides resource dependence theory, the agency theory argues that the gap and conflicts between the principals and agents (Agency conflicts type I) can be resolved via the frequency of RMC meetings held during the year. It is established that the more meetings an RMC holds during the year, the better the communication between the parties involved in risk oversight. According to the studies of [26, 27] a sufficient number of meetings will allow for an in-depth discussion of key risk-management issues such as “risk appetite, risk avoidance, and risk awareness”. therefore, the frequency of meetings reflects the diligence of the RMCs.

### 2.1.3. The RMC Overlap and Corporate Financial Performance

RMC overlapping refers to the proportion of the RMC

members who have at least two functions on different board committees such as the remunerations committee or audit committee. According to Faleye, et al. [28] overlapped and independent members on the board can use further information to achieve a better understanding of the company, which leads to better performance. Hines, et al. [29] argue that corporations with overlapping directors sitting in different board sub-committees report a higher quality of accounting information and bear lower audit fees. Consistently, Coles, et al. [30] provided an empirical evidence on the overlapping of board members and their effects on the firm value. The study utilizes a data of 1500 US listed-firms the period of 1996-2014 and questions “do overlapped directors influence the firm value”. Their findings indicate that the overlapped directors have a positive influence on the firm value in complex firms and teamwork.

### 2.1.4. The RMC Qualification and Corporate Financial Performance

The competence of a director, in addition to the factors mentioned above, is also a significant factor in ensuring that the board and its sub-committees work effectively. Given the resource dependency theory, directors with higher experiences, and more skills can help in constraining earnings management practices [31]. One of the indicators of the competence of the director is his qualifications and experiences. In addition, the investors tend to invest in businesses that have a large number of trained and qualified board members. In the case of RMCs, members equipped with the appropriate qualifications and experiences are capable of identifying and addressing the corporation’s problems and challenges. A study conducted by Al-Hadi, et al. [18] used a sample of 677 observations from gulf council cooperation from 2007 to 2011. The study question “whether the existence of a separated RMC with qualified members is associated with market risk disclosures and firm life cycle stages”. The study found that competent and qualified members sitting in the RMC can participate in adding value to the business by mitigating uncertainties and taking responsible actions in managing the business’s challenges and problems. Aldhamari, et al. [8] examine the effects of the RMCs effectiveness (using qualified directors as one of the factors) and corporate financial performance using a sample of financial firms listed in the Malaysian market from 2004 to 2018. The results indicated that qualified RMC members have a significant positive impact on corporate performance.

## 2.2. Risk Management Committee and Financial Reporting Quality

Previous researchers have documented that RMCs play important roles in the effectiveness of corporations because as board-level committees, they are at the top level of management. Recent global financial scandals

have shed light upon the important role of risk management in efficient corporate governance in various markets around the world. Spira and Page [32] have suggested a reinvention in the firms' risk management efforts since internal control and internal audit play a vital role in strategies for risk management. This study has turned into a review of the previous researches on the demographic attributes of RMC and its effects on the quality of financial reporting.

Subramaniam, et al. [1] use the sample of 200 top ASX-listed companies in the year 2005, to examine how the RMC functions. The authors observe that having a stand-alone RMC that is separated from the AC is more likely to enhance the governance practice and financial reporting quality. Ng, et al. [4] analysed the data obtained from 329 Malaysian firms using the period 2003-2011. The central focus of the study was "to what extent the RMC can monitor and influence the underwriting risk of the firms". The study concluded that RMC plays a significant negative role in firms' underwritten risk that

has a relationship with the going concern. Abdullah, et al. [14] provide evidence that the RMC has a fundamental role in influencing the level of hedging activities and information disclosure which consequently can reduce the management's desire to use hedging to manipulate earnings. Kallamu [7] uses sample data of 37 firms listed in the Malaysian stock market from 2007 to 2011, the study indicated that the existence of a separate RMC has positively influenced market valuation as well as accounting return. According to the study done by Wu, et al. [15] the RMCs of listed companies in Malaysia influence the efficiency level of the firms. More recently, Mohd-Sanusi, et al. [33] conclude that the existence of an RMC enhances the awareness of enterprise risk management (ERM) within corporations which will as a result increase their market value. The evidence presented is in line with the idea that a company that has poor-risk oversight is more likely to have a loss in the shareholders' fund.

**Table 1.** Summary of Empirical Studies on Risk Management Committee Attributes.

Author	Country-scope	Dependent variable	Independent variable	Results
Ames, Hines, Sankara, & Policy, (2018) [36]	US (2007-2013).	-A.M. Best's Financial Strength Ratings.	Existence of board RMC	Positive-significant
Abdullah, Ismail, and Izah (2016) [37]	Malaysia (2013)	-Hedge Accounting Practices	RMC Effectiveness	Non-significant
Subramaniam, McManus (2009) [1]	Australia (ASX for the year 2005)	-Governance practices -Financial reporting quality	Stand-alone RMC	Positive-significant Positive-significant
Bhuiyan,Salma, Roudaki, & Tavite, (2020) [19]	Australia (ASX 2001-2013)	-Financial reporting quality -Audit pricing.	Existence RMC	Positive-significant Positive-significant
Kallamu (2015) [7]	Malaysia (2007-2011)	-Firm market valuation -ROA	RMC independent	Positive-significant Negative-significant
Jia, (2019) [17]	Australian stock exchange (2007-2014)	-Financial distress	RMC gender	Negative-significant
Abdullah and Said (2019) [3]	Malaysia, (2002-2014)	-The prevention of corporate financial crime	Separated RMC	Positive-significant
Ali, Besar, and Mastuki (2017) [38]	Malaysia (2005-2015)	-Financial restatement practices	Existence of RMC	Negative-significant
Tao, Hutchinson, (2013) [39]	Australia (2006-2008)	-Information asymmetry	RMC overlap	Negative-significant
Jia & Bradbury, (2020) [40]	Australia (2007-2014)	-Distress probability. -Growth options. -ROA.	Existence of RMC	Negative significant Positive significant Positive significant
Malik, Shafie, Ku ismail (2021) [41]	Malaysia (2015-2017)	-Tobin's Q (Market performance).	-RMC-size -RMC Independent -RMC Expertise -RMC Gender	Negative significant Negative significant Positive significant Negative significant

Furthermore, Sani, et al. [34] in the context of Nigeria use data of 400 firm-year observations covering the period of 2012- 2016 to determine the influence of RMC on sales manipulation (a real earnings management practice). The findings indicate that the presence of an RMC reduces management's desire to engage in manipulating the reported earnings through. Abdullah and Said [3] used data of financial crime cases reported by Malaysian SC for the period of 2002-2014, and question “whether there is an association between the presence of a stand-alone RMC and corporate financial crimes”, the study concluded that the RMC mechanism has significantly and negatively influenced the cases of corporate financial crimes. The interpretation from this result is that the formation of an RMC will assist the firms in meeting their targets, secure their reputation, and improve their FRQ. A study conducted by [17] examined the influence of RMC diversity on a corporate’s probability of getting financial distresses using a sample of top 300 ASX listed companies the period of 2007-2014. The researchers revealed that the presence of RMC’s female members enhanced the monitoring of the risk management function and reduced the excessive risk-taking behaviours of companies which, in turn, reduce the probability of getting financial distresses. More recently, a study done by [35] recommends that additional attention must be given to governance mechanisms, including the function of risk committees, to reduce manipulation of earnings and improve reporting quality.

### 3. Research Methodology

RMC attributes are a very important topic since the RMC is one of the influential board committees, the committee is able to perform the oversight of the corporate’s risk management framework and policies and enhance the information transactions between board

committees. As a result of the importance of this topic, the aim of the current paper is to determine to which extent the RMC and its attributes influence corporate performance and FRQ. The paper concentrates primarily on the RMC demographic attributes to limit the scope of the review. In order to guide the literature search, we established some criteria for the articles to be reviewed: (i) online peer-reviewed, research papers or dissertations published in international conferences and journals, and international venues. (ii) research papers that focused mainly on any of the RMC attributes and its influence on financial reporting quality or firm performance. (iii) research papers that described the procedures and methodologies utilized to conduct the studies (e.g., quantitative or qualitative approaches). (iv) this review excluded theoretical discussions that concentrated on RMC attributes without empirical evidence. In addition, relevant studies for this paper were found by searching online databases including “Science Direct, Google Scholar, Scopus, ProQuest, EBSCOhost explores, and Emerald Insight”. The literature search was performed using the following keywords: “RMC characteristics”, “RMC demographics characteristics”, “RMC features”, “firm performance”, “RMC attributes”, “financial reporting fraud”, “earnings management”, “corporate financial performance” and “financial reporting quality”. The criteria mentioned above resulted in 128 research papers in the first mining. out of these 128, the review identified 38 articles that dealt with the impact of RMC attributes on FP and FRQ, which have been published from 2003 to 2021 in leading and prominent journals and conferences in the areas of accounting, management, business, and finance. The articles have been searched and sorted based on the RMC's attributes and its relation to “corporate financial performance and financial reporting quality”. Figure 1 shows a graphic representation of the methodology review for this paper.

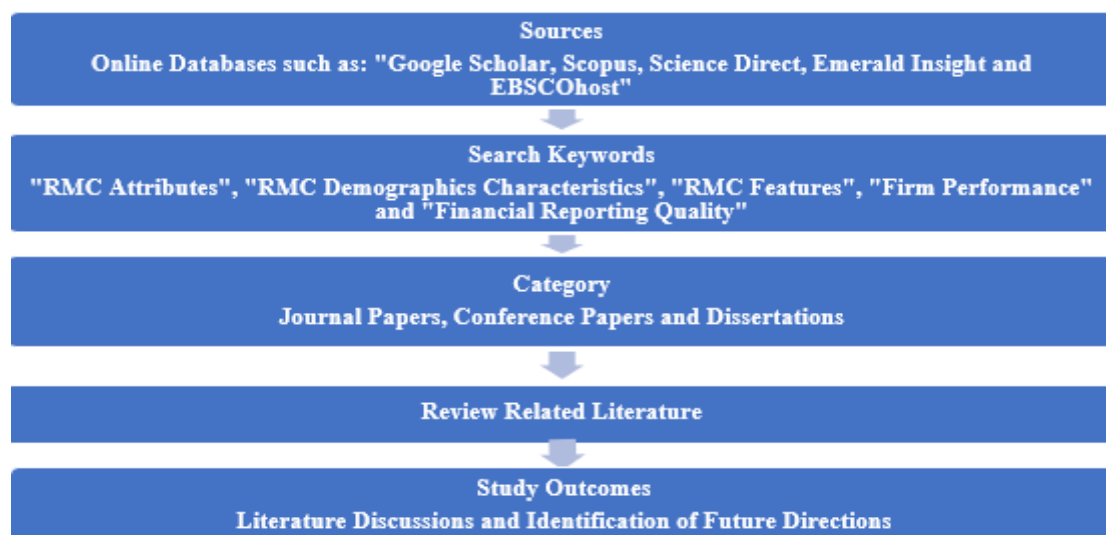


Figure 1. Reviewing the methodology

## 4. Discussion and Conclusion

The primary objective of this paper has been to review existing empirical studies that examined the impacts of RMC demographic attributes on both corporate performance and FRQ measurements. Therefore, the review is anticipated to promote the understanding of researchers and policymakers concerning the functions of RMC mechanisms. Overall, the outcomes of this review demonstrate that the roles of RMC attributes have influences on the corporation's financial performance as well as on its reporting quality.

Based on reviewing the RMC empirical studies, it is evinced that RMC attributes, such as: "the existence of the RMC itself, the financial expertise of its members, as well as its committee size and the presence of independent members" are able to contribute to high-quality financial information and corporate financial performance. Hence, it is worth noting that such experience may positively help in strengthening the performance of corporations and enhancing their financial reporting process, which can also reduce the irregularity of information between the corporation and its stakeholders. Besides, the independence of RMC members is expected to withstand any pressure and obtain the necessary information from managers to control the risks which will result in enhancing corporate performance, in addition to enhancing the capabilities of board members.

Furthermore, this review reveals that the RMC overlapped members that have membership in other committees can improve the company's performance and mitigate potential risks. Likewise, the study indicates that RMC members that are equipped with adequate knowledge can understand, and handle the challenges and problems the businesses may face. However, the results of all the aforementioned studies were mixed and inconclusive which created a research gap, especially in this area. Based on the review, several gaps in the literature have also been identified as a result of the inconsistent findings of prior researches. Subsequently, in order to fill these gaps, the following suggestions are presented for future research.

The literature examination regarding the effects of RMC attributes on corporate performance and reporting quality has shown some promising directions and research opportunities for future studies even though the review outcomes need to be interpreted meticulously. In addition, the relationships between RMC attributes and corporate performance are not decisive. researchers in the future may take into consideration the findings of this review and examine further the roles of RMC attributes on FRQ by using different measurements of the latter, including "earnings smoothing, volume estimation of pension obligation discount rates, financial restatements, financial irregularities, earnings persistence, and earnings forecasts". Although some improvement has been achieved to better understand the relationship between RMC attributes and corporate results, further research on such a ripe area is needed.

Furthermore, a review of the prior empirical studies cited here indicates that the results on the impacts of RMC attributes on lower FRQ are still inconclusive. Some researchers found a positive association such as [17, 39], although others found no association at all [37]. The mixed and inconclusive findings of previous studies perhaps owing to the differences in the measurements used in these studies or the timeframe they choose. As a result, the relationship between financial reporting quality and RMC attributes remains unclear. In addition, more research is needed to see whether RMC attributes are associated with fraudulent financial statements, or whether RMC attributes influence the corporate's long-term sustainability. While this area is critical to the body of knowledge as well as policy setters especially after the fraud cases that happened in different countries in previous years, it could be considered as a new topic for researches in the future due to the lack of studies to date. Other attributes that would influence the FRQ and corporate performance, such as: RMC interlocking, RMC certification, RMC risk-expertise, and RMC training, may be considered in future studies. hence, as will be shown in Table1, the current review presents a variety of questions, that in our view, need further investigations in the future.

**Table 2.** Recommendations for RMC Attributes Future Directions

No	Research Questions
<b>RMC Attributes and Corporate Financial Performance</b>	
R.Question1	How do RMC attributes important to corporate financial performance?
R.Question2	How do risk management committee attributes (RMC interlocking, RMC qualification, RMC risk-expertise, and RMC training) affect corporate financial performance?
<b>RMC Attributes and Financial reporting quality</b>	
R.Question3	How does the RMC attributes influence the financial reporting quality "earnings smoothing, discount rates, financial restatement, financial irregularities, earnings persistence, and earnings forecasts"?
R.Question4	How do risk management committee attributes (RMC interlocking, RMC qualification, RMC risk-expertise, and RMC training) influence financial reporting quality?
R.Question5	Do RMC attributes influence Real Earnings Manipulations?
<b>RMC Attributes and Fraudulent Financial Statements</b>	
R.Question6	How do RMC attributes influence fraudulent financial statements?
R.Question7	How does RMC deal with fraudulent financial statements?
<b>RMC Attributes and Corporate Sustainability</b>	
R.Question8	How do RMC attributes influence the corporate's sustainability?
R.Question9	What are the important RMC attributes that may influence the corporate's sustainability?

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