

# *Executive Summary*



### *Interview insights*

Our industry is currently suffering from significant government and regulatory interference. Accordingly, many companies and audit committees are focusing on rules and compliance. We need to be more balanced and refocus our attention back on the business.

– AC Chair

The global capital markets rely heavily on the quality of financial statements. The economic crisis that started in 2008 increased the focus on both the role of the audit committee and the information companies disclose. The audit committee's role in ensuring accurate and transparent disclosure is more important today than it has ever been. Clearly, the job is also more difficult and challenging than ever — given increased expectations by shareholders, regulators, and other stakeholders; heightened scrutiny when things go wrong; more responsibility for risk management; and more focus on the need for fraud prevention.

The bottom line is that people expect more from audit committees today, and this publication provides insight into audit committee leading practices that can help committees meet those expectations.

### *What the chapters cover*

#### **1. Financial Reporting and Disclosures**

Financial reporting disclosure requirements have been steadily increasing for a number of years, in tandem with the complexity of accounting standards. Regulators and financial statement users continue to press companies for more

information and to get that information sooner. This environment makes the audit committee's responsibility to oversee the company's financial reporting more difficult. The committee must be aware of the financial reporting risks to focus its attention appropriately. And it cannot lose sight of the need to maintain its skepticism. This chapter highlights ways the committee can best understand and monitor the company's financial reporting.

#### **2. Risk Management and the System of Internal Control**

Given how many risks — known and unknown — a company faces, it's a challenge for a board or audit committee to get comfortable that the company is addressing risk appropriately. One of the difficulties facing the audit committee is clearly defining its risk responsibility relative to that of the entire board. While the company's system of internal control is designed to help mitigate risk, the audit committee focuses particularly on controls relating to financial reporting, fraud, and compliance. This chapter helps the committee to better understand the risks that most likely fall within its scope and how to monitor whether the company is addressing those risks appropriately.

### ***3. Culture and Compliance — The Soul of Corporate Accountability***

The company's culture and code of conduct are critical factors in creating an environment that encourages compliance with laws and regulations. The audit committee must recognize how critical the right tone at the top of the company is and ensure what it's hearing in the boardroom is what employees are hearing throughout the company. This chapter provides insights that help the committee understand what elements compliance programs should have to promote proper conduct and behavior throughout the company.

### ***4. Oversight of Management and Internal Audit***

The audit committee needs to oversee management while taking care not to step into management's role. Establishing an effective relationship with management is essential — it allows the committee to effectively monitor the company's financial reporting practices and evaluate management's competence. Similarly, the committee relies heavily on internal audit to provide an objective view on how the company is handling a number of key risks, including those relating to financial reporting and compliance. This chapter discusses how the committee builds effective relationships with both management and internal audit.

### ***5. Relationship with External Auditors***

The audit committee has to select the right external auditors to conduct a quality audit. As part of executing their audit plan, the external auditors provide the audit committee with assurance regarding the company's financial reporting. Additionally, external auditors are in a unique position to provide unfiltered and unbiased feedback to the committee about management and the company's processes. This chapter guides the committee through the ways to evaluate and appoint auditors and to develop and maximize the value of external audit relationships.

### ***6. What to Do When Things Go Wrong — Financial Statement Errors and Fraud Investigations***

At times, breakdowns in financial reporting processes lead to potential errors in previously issued financial statements. Management and the audit committee have to assess whether an error is material and, if it is, take steps to resolve the situation. The situation can become more complex if the error results from fraud. The committee also might have to become involved when allegations arise of bribery or other forms of fraud. In such cases, the committee may have to oversee an investigation. This chapter discusses factors for the committee when it must consider a possible restatement or oversee an investigation.

### **7. Committee Composition**

Composition and leadership are critical in supporting the audit committee's ability to carry out its responsibilities effectively. The committee needs the right combination of skills and experience. It also needs a chair with the knowledge and commitment to drive the committee's work. This chapter discusses considerations for selecting committee members and the chair and for determining how large the committee should be.

### **8. Meetings**

To ensure committee meetings run well, the committee needs to have the right agenda and receive the right materials beforehand. The attendees, and how they interact with committee members, also influence the success of meetings. Given how many responsibilities the committee has, it needs to ensure it is meeting often enough and at the right points during the year. This chapter describes ways the committee can create an effective meeting environment, allowing the members to engage in meaningful discussion and make the most of private sessions.

### **9. Supporting Committee Effectiveness — Charter, Evaluations, Resources, and Training**

The charter documents the audit committee's purpose, roles, and responsibilities. It helps distinguish the committee's responsibilities from those of the full board of directors. An audit committee that periodically evaluates its performance will be able to identify ways to improve its effectiveness. Orientation training for new members and ongoing development for all members are essential, particularly given the velocity of changes to financial reporting and governance standards. This chapter discusses considerations for the committee's charter, methods the committee can use to assess its performance, and ways to meet its training objectives.