

Audit Committees: An Often Overlooked Resource

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Audit committees by nature are not glamorous, and seem to have earned necessary-evil status at most companies. However, an audit committee can be a very effective tool to ensure proper and consistent financial reporting. Whether your company has an audit committee or is thinking about forming one, now is a good time to consider its advantages and effective operation. In this article, we will examine basic provisions of an audit committee charter, selection of audit committee members, and how to use these resources to benefit financial reporting and ultimately contribute to the success of a company.

Establish committee parameters

The first step in creating an audit committee is to adopt an audit committee charter. Audit committee charters can range in length, detail and content, but should include several basic provisions. For example, an audit committee charter should determine how many members will serve on the audit committee and mandate that members be independent. It is critical to ensure that an impartial objective committee is reviewing the financial statements and related audit reports, as well as any other reporting issued by the company, and that there are no potential conflicts of interest. The charter also should address how many times per year the committee will meet. This will vary depending on the size and complexity of the company; smaller, less complex companies will likely meet fewer times per year than larger, more complex companies.

A critical function of the audit committee is to oversee a company's internal controls and risk management procedures. Key charter components that address internal controls and risk management include reviewing and evaluating the performance of independent auditors; inquiry of management and independent auditors about significant risks or exposures facing the company, and what steps are taken to reduce these exposures; as well as review with management and independent auditors about the adequacy of the company's internal controls.

The audit committee charter also needs to address the application of accounting and regulatory standards. It should include provisions that require review with management and independent auditors regarding the effects of any regulatory and accounting initiatives, all critical

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accounting policies and practices and any alternative treatments of Generally Accepted Accounting Principles. Proper review also should include examination of written communications between the independent auditors and management.

Focus on financial statements

The next area the audit committee charter needs to address is the review of the company's financial statements. The charter should include provisions to review with management and independent auditors the company's annual financial statements, audit report and related footnotes. The charter also should address review of the independent auditor's judgments about the quality of application of accounting principles, any significant changes to the audit plan, any serious difficulties or disputes with management that were encountered during the audit, and matters that are required to be discussed by Statement on Auditing Standards No. 114, The Auditor's Communication With Those Charged With Governance..

The final area the audit committee charter should address relates to legal matters and compliance with internal codes of conduct. In order to properly address these issues, the audit committee charter should include a review with general counsel and management of any legal and regulatory matters that would have a material impact on the financial statements. The charter also should cover periodic review of the company's code of conduct to ensure its adequacy and applicability; review of procedures for receipt, retention and treatment of complaints received by the company regarding accounting or internal controls; and review of procedures for employees' confidential submission of concerns regarding questionable accounting or auditing matters.

Now that we have discussed the audit committee charter, we need to focus on the audit committee itself. The audit committee should be composed of an odd number of people in order to avoid ties on matters requiring a vote. It is very important to select the right mix of members. Ideally, the committee will include members from the banking, legal and accounting professions. This will ensure that all areas of the audit committee charter, risk management, internal controls, accounting and regulatory procedures, and compliance are properly addressed by members with proficiency in those areas.

A valuable asset

In conclusion, an audit committee can be a critical oversight mechanism, especially during difficult times when the level of scrutiny is much higher and requires more oversight. Having an audit committee does not have to be a burden to your company. It can be an effective, useful tool to

AUDIT COMMITTEE BRIEF

From the Audit Committee Effectiveness Center

For more information:

Statement on Auditing Standards No. 114, The Auditor's Communication With Those Charged With Governance
aicpa.org/download/members/div/auditsd/AU-00380.PDF

Audit Committee Toolkits:

Public Companies

cpa2biz.com/AST/Main/CPA2BIZ_Primary/FinancialManagement/Management/AuditCommittee/PRDOVR~PC-991001/PC-991001.jsp

Private Companies

cpa2biz.com/AST/Main/CPA2BIZ_Primary/FinancialManagement/Management/AuditCommittee/PRDOVR~PC-991007/PC-991007.jsp

Not-for-Profit Organizations

cpa2biz.com/AST/Main/CPA2BIZ_Primary/AuditAttest/AuditPreparationandPlanning/PRDOVR~PC-991004/PC-991004.jsp

Government Organizations

cpa2biz.com/AST/Main/CPA2BIZ_Primary/AuditAttest/AuditPreparationandPlanning/PRDOVR~PC-991005/PC-991005.jsp

ensure your company is properly and consistently applying accounting and regulatory principles, effectively managing risk exposure and creating a strong culture of internal control.

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http://www.cpa2biz.com/AST/Main/CPA2BIZ_Primary/AuditAttest/PRDOVR~PC-NACF/PC-NACF.jsp

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