

Audit Committees: The Roles and Responsibilities

While audit committees are not required for all organizations, those who use one – or plan to form one – should pay close attention to how audit committees operate.

What is an audit committee?

The primary purpose of an audit committee is to provide oversight of the financial reporting process, the audit process, the system of internal controls and compliance with laws and regulations.

The audit committee can expect to review significant accounting and reporting issues and recent professional and regulatory pronouncements to understand the potential impact on financial statements. An understanding of how management develops internal interim financial information is necessary to assess whether reports are complete and accurate.



The committee reviews the results of the audit with management and external auditors, including matters required to be communicated to the committee under generally accepted auditing standards.

Audit committees will consider internal controls and review their effectiveness. Reports on, and management responses to, observations and significant findings should be obtained and reviewed by the committee. Controls over financial reporting, information technology security and operational matters fall under the purview of the committee.

**GELMAN, ROSENBERG
& FREEDMAN**

CERTIFIED PUBLIC ACCOUNTANTS



4550 Montgomery Avenue, Suite 650N • Bethesda, MD 20814
(301) 951-9090 • Fax: (301) 951-3570 • www.grfcpa.com

Personal Attention Will Never Become Obsolete



How does an audit committee work?

The committee establishes procedures for accepting confidential, anonymous concerns relative to financial reporting and internal control matters. Often referred to as a “whistle-blower policy,” the procedures allow individuals to bring questions and issues to light without fear of retribution.

The audit committee is responsible for the appointment, compensation and oversight of the work of the auditor. As such, CPAs report directly to the audit committee, not management.

Audit committees should meet separately with external auditors to discuss matters that the committee or auditors believe should

be discussed privately. The committee will also review the proposed audit approach and handle coordination of the audit effort with internal audit staff, if applicable.

When an internal audit function exists, the committee will review and approve the audit plan, review staffing and organization of the function and meet with internal auditors and management on a periodic basis to discuss matters of concern that may arise.

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What do audit committee members do?

Committee members can expect to participate in an executive session at each meeting. These sessions can be used to meet with auditors, key members of management or financial reporting staff and provide the opportunity to glean candid information on potentially sensitive topics.

A recent survey of audit committee members reveals that a key focus has become enterprise risk management (ERM). Those surveyed ranked the level of challenge related to enterprise risk management significantly above governance, risk management, financial reporting and internal audit.



The reason is simple. ERM embraces every risk perspective of an organization. While the entire board is responsible for enterprise risk management, the ownership may rest with the audit committee. Audit committees should re-examine focus, monitor effectiveness and set the course for future activities. Newly formed committees can benefit from the wealth of experience offered by those who have spent time in the trenches.



Effective internal control emanates from the top and permeates throughout an organization. Senior management must set the tone for internal control and the audit committee can be an important piece in the internal control puzzle.

All too frequently in the past, audit committees were stacked with cronies of the chairman and president. They tended to be rubber stamps of the chief executives that met the letter, but certainly not the spirit, of the rules. In such an environment, they tended to

disguise control rather than contribute to it.

However, an audit committee established with the proper attitude and responsibility will accomplish exactly that. If you're a skeptic, you naturally may wonder how more bureaucracy can contribute to profits.

What is an audit committee charter?

An audit committee charter sets forth the general purpose, authority, composition and responsibilities of the committee. The charter should be tailored to the organization.

On an annual basis, the committee should determine that all responsibilities outlined in the charter have been carried out. In addition, the charter should be reviewed and proposed updates presented to the board for approval.

While the charter must remain effective, so must committee members. Best practices include an annual evaluation of members' performance.



Although audit committees may be reluctant to focus on self-measurement for fear of disclosing weaknesses, evaluation of committee activities is a key tool in achieving and maintaining a high degree of effectiveness.

What are the benefits of an audit committee?

Good management involves matching key tasks with the appropriate people to achieve better results. Your company can derive the most benefit from an audit committee by following these five steps:

1. Leverage your time. Financial reporting is becoming more important and complicated every year. An audit committee should be led by a designated “financial expert” and staffed with a select group of people knowledgeable about financial matters.



2. Improve your internal control. Internal control may not be at the top of your list of important objectives but it should be. Internal control is more than dual signatures on checks and segregation of duties. Properly designed, it will support every aspect of your company.

Proper internal controls will lead to higher efficiencies in all processes, less waste of resources, more objective evaluation methods and more timely and accurate management measurements. Think how valuable such improvements would be for your organization and how much you would be willing to pay a consultant to guide you in the right direction. This is another role an effective audit committee can fill.



3. Improve your financial management. The audit committee focuses on the financial management and reporting of the company. This group provides a high level of specific expertise in this critical area of your company.

Financial management and reporting determine your credit-worthiness to outsiders and growth targets and successes to insiders. They are the key determinants in establishing the market value of your company – the ultimate scoreboard for management’s results.

Does your board actively manage your company’s financial and reporting functions – or delegate them to the outside auditor? You and your board have the responsibility and are held accountable for these functions.

4. Clarify the roles and responsibilities of your board of directors. A common myth is that a company can get by without an audit committee. The board of directors may be responsible for doing the work of an audit committee.

But without clear responsibilities assigned, there is the risk that the task may be inefficiently or ineffectively executed or perhaps not executed at all. Having a separate audit committee clarifies key responsibilities for your board.

5. Bring value to your audit dollar. An audit is an expensive endeavor that all too many view as a “necessary evil” or another cost of borrowing. An active audit committee stays involved with the auditors throughout the year. The audit committee’s relationship with the auditor is similar to a willing and engaged patient who makes the physician better and more effective. Hidden problems can be discovered early and dealt with before they grow into something dangerous.

