

# Effectiveness of an audit committee



An audit committee plays a pivotal role in ensuring corporate governance of a company through performance of its core duties which essentially involves - oversight of a company's financial reporting process, monitoring the auditor's independence and performance and approval of a company's transactions with the related parties. The oversight responsibilities extend to cover a range of other risks including technology risks and other operational and

compliance risks posed by the extended organisation (vendors, suppliers, etc.). Prioritising this heavy committee workload is one of the constant challenges being faced by the audit committees. Therefore, there is a need to focus on defining ways in which an audit committee can discharge its responsibilities effectively and efficiently.

**No one size fits all, yet we believe that certain principles are key to effectiveness of every audit committee.**



## 1. Reinforce the right audit committee culture

Critical factors that can contribute to the enhanced effectiveness include knowledge, experience, independence of audit committee members, the extent and quality of committee's interactions with the management and auditors (external and internal) and most importantly, the committee's leadership. Key considerations for an audit committee chair are:

- Ensure that the committee has the right mix of people with expertise, knowledge and professional and personal attributes that are crucial to the business in which a company operates.

*There might be less possibility of differing attitude and values, but the knowledge level of audit committee members can vastly differ.*

- Minimum attributes to be possessed by members include - integrity, trustworthiness, sound judgement and professional skepticism, including a willingness to probe and ask tough questions.
- Demonstrating effective leadership requires an audit committee chair to have a clear understanding of the committee's duties and responsibilities, be readily available on urgent matters and in times of crisis. Additionally, should possess requisite business, financial, communication and leadership skills.

*Role of AC chair – Requires attached detachment – attached to the company and at the same time be detached from the company. One needs to take interest in the company but ensure you are not part of the management.*

## 2. Setting the agenda

Prepare a focused agenda allocating significant time to the company's key financial reporting risks and other matters that require the audit committee's attention. While input from management and the internal and external auditors are crucial, the committee should not merely adopt an agenda prepared by the management of the company.

*An audit committee should have full control of its agenda. If something is being added or deleted from its agenda without audit committee's permission, then authority of an audit committee is being challenged.*

Some of the key considerations for an effective audit committee agenda include:

- Consider priority items (including those that are mandatorily required by regulations) followed by

routine and other matters. Avoid overloading of items and if necessary, consider a separate meeting for significantly less important areas.

- Discuss agenda with the CFO, head of internal audit and others as appropriate particularly on the key issues to be considered, time to be allotted on each of the agenda topics and who all should participate in the discussion of each topic.
- Share the draft agenda with other committee members and encourage them to provide their inputs including suggestion on follow-up items for future committee meetings.

*One cannot templatised the agenda items; but an audit committee agenda should ensure full coverage of aspects required by the charter of the committee.*

## 3. Effective audit committee meetings

Preparation and active participation of the committee members is key to an effective audit committee meeting. Foster an atmosphere of open and transparent expression of thoughts with reasonable opportunity to pose questions to the management, auditors, and other key participants. Further, consider the following:

- Insist on quality pre-meeting materials and go through them before the meeting.
- Balance presentation time with time for discussion and questions.

*Ensure auditees make the presentations to the audit committee rather than CFO anchoring those presentations. Technical matters should be communicated in a practical business language for a better understanding of all the participants in the meeting. Make formal presentations as they stay on record.*

- CEO's presence in committee meetings can place greater accountability on the management and can act as a catalyst for action. Though an audit committee needs to be alive to possibility that a CEO's presence could, in some instances, hamper a free and frank exchange of views especially for persons- within the company- junior to the CEO.
- Follow up on the unresolved issues that were discussed at the previous committee meetings; allow time for forward-looking discussions on strategy and risk.
- Committee members should be made aware of deliberations from any external/informal interactions by an audit committee chair.
- Conclude (or sometimes begin) each meeting with an executive session so that members have an opportunity to discuss important matters privately without management's presence.



#### 4. Align audit committee's responsibilities with other committees

Lack of clearly defined terms of reference vis-à-vis other committees of the company, in particular, the risk management committee is a constant challenge.

*There are potential overlaps with risk management committee which needs to be finetuned.*

Effectively coordinate an audit committee's terms of reference with that of other committees in the company which might be required to consider the same issue from some different perspectives.

Acknowledge that risk oversight is a full board function. While in practice, various aspects of risks could have been

allocated among different board committees to reduce the burden on the audit committee e.g., CSR committee or technology committee. Possible approaches to improve coordination and reduce the risk of a divided structure include:

- Clear and robust communication of risk oversight responsibilities of the board and its committees.
- At least one member of the committee serves on the risk management committee and other board committees and vice versa.

*Reciprocal membership facilitates better decision-making.*

#### 5. Setting expectations for internal and external auditors

Effective oversight of internal and external auditors is at the core of audit committee's responsibilities.

##### External audit

To facilitate performance of their oversight responsibilities vis-à-vis external auditors, an audit committee should ensure the following:

- Assess qualifications, expertise, resources, and independence of external auditors
- Assess the independence and objectivity of the auditor considering applicable laws and regulations
- Assess the effectiveness of the audit process giving due consideration to the overall audit work plan, level of materiality and resource allocation being consistent with the scope of engagement
- Monitor management's responsiveness to the auditor's findings and observations during the audit process.

##### Internal audit

An audit committee can help internal audit add value to the company by:

- Making sure that the internal audit has the necessary skills (e.g. IT experience, cross-functional trainings, risk management and evaluation, etc.).

*Internal audit function should comprise of people from various departments – procurement, sales, marketing, HR so that respect and acceptability of the function goes up.*

- In case the internal audit function is outsourced/co-sourced, ensure active involvement in the proposals for such outsourcing/co-sourcing and continue to provide oversight of the outsourced services.
- Reinforcing internal audit's stature within the company and clearly defining its accountability to the audit committee. Encourage open and transparent communication between the audit committee and head of internal audit.



## 6. Proper and timely documentation

Ensure proper documentation of the proceedings covering important decisions taken during the committee's meeting for effective performance of its oversight responsibilities. Committee members are also encouraged to pen down important points discussed in the meeting for their future reference.



*It is good to have your noting documented as much as possible—formally communicate with the company in an email so that you are most effective in the recorded manner.*



There may not be defined mechanics or a single approach to enhance performance of an audit committee but addressing some of these recommendations could help members to effectively discharge their responsibilities.

We would like to thank our Audit Committee council members for their time in providing us with their valuable insights and perspectives that have contributed to building this PoV document.

Audit Committee Council Members: Ms. Geeta Mathur, Mr. Milind Sarwate, Mr. M.D. Ranganath, Mr. Narayanan Kumar, Ms. Revathy Ashok, Ms. Sudha Pillai, Mr. Vivek Gour.

## KPMG in India contact:



### Ritesh Tiwari

Partner,

Risk Consulting

Leader, Board Leadership Center

KPMG in India

T: +91-8588862899

E: riteshtiwari@kpmg.com

[home.kpmg/in](https://home.kpmg/in)

#KPMGjosh

Follow us on:

[home.kpmg/in/social-media](https://home.kpmg/in/social-media)



The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

KPMG Assurance and Consulting Services LLP, Lodha Excelus, Apollo Mills Compound, NM Joshi Marg, Mahalaxmi, Mumbai - 400 011 Phone: +91 22 3989 6000 Fax: +91 22 3983 6000

© 2021 KPMG Assurance and Consulting Services LLP, an Indian Limited Liability Partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

KPMG (Registered) (a partnership firm with Registration No. BA- 62445) converted into KPMG Assurance and Consulting Services LLP (a Limited Liability partnership firm) with LLP Registration No. AAT-0367 with effect from July 23, 2020.

The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization.

This document is meant for e-communication only.(007\_FLY0621\_DGR)