

# THE BULLETIN

OUR VIEW ON CORPORATE GOVERNANCE MATTERS

## Assessment Questions for Audit Committees to Consider

(Offered in Conjunction With Protiviti's *The Bulletin*,  
"Setting the 2023 Audit Committee Agenda"<sup>1</sup>)

The following questions are provided to assist audit committee members in their assessments of committee composition, agenda and focus in view of the company's industry, circumstances, risks, financial reporting issues and current challenges it may be facing. These questions are intended to be illustrative and do not purport to cover every topic the committee should consider, nor are they intended to be a one-size-fits-all approach that applies to every audit committee. The full list of questions may be better suited to larger companies. Accordingly, they should be customized to the committee's specific needs and assessment focus, in conjunction with the board's overall self-assessment process. These questions should be used in conjunction with the agenda items suggested in Protiviti's latest issue of *The Bulletin*, "Setting the 2023 Audit Committee Agenda," as those items are unique to the next 12 months and may not be included specifically in this summary.

### Committee Composition and Dynamics

- Do all members of the committee meet the applicable independence requirements? For example, committee members cannot receive additional compensatory income outside of director fees, have family members serving in senior executive positions, or be affiliated with the company, its subsidiaries or the independent auditor.

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<sup>1</sup> "Setting the 2023 Audit Committee Agenda," *The Bulletin*, Volume 8, Issue 3, December 2022, Protiviti:  
[www.protiviti.com/US-en/newsletter/bulletinv8i3-2023-audit-committee-agenda](http://www.protiviti.com/US-en/newsletter/bulletinv8i3-2023-audit-committee-agenda).

- Do committee members have the requisite business and leadership experience, and is the committee's composition sufficiently diverse to oversee the financial reporting process, expanded emphasis on disclosing nonfinancial information to investors and other relevant issues germane to the committee's chartered activities?

The following questions should be considered with respect to composition:

- Are all members of the committee financially literate (e.g., are they capable of reading and understanding the financial statements)?
- Is at least one audit committee member an expert in financial reporting matters germane to the issues the company faces in preparing financial reports in accordance with applicable accounting standards?
- Does the committee have access to other sources of expertise beyond financial reporting needed to fulfill its responsibilities (e.g., technology, cybersecurity and regulatory matters)?
- Are committee members, including the chair, periodically rotated to encourage fresh perspectives in discharging the committee's responsibilities?
- Are the frequency and duration of committee meetings sufficient to permit active discussions with management and other executives?
- Does the committee engage independent advisers when they are needed?
- Does the committee coordinate its activities with other board committees to ensure sufficient board oversight coverage of significant matters?

## **Committee Charter and Agenda**

- Does the committee review and approve the charter and align its activities with a calendar that incorporates required activities and allows flexibility to cover additional topics as they emerge?
- Are the committee charter and agenda focused on the issues most likely to affect the quality of financial and other information reported?
- Are meeting agendas developed in consultation with management and the external auditor?
- Are committee meeting materials and agendas aligned with priority areas?

## **Oversight of Internal Controls and Financial Reporting**

- Do committee members understand the processes for identifying key controls and reporting risk areas used by management, the internal auditors and the independent auditor?
- Does the committee focus its oversight on understanding high-risk and complex accounting and reporting areas — particularly areas involving significant judgment and estimation processes — and how management addresses them and their financial statement impact?

- Does the committee understand the major issues raised in comment letters the company receives from the Securities and Exchange Commission (SEC) and management’s planned response?
- Does the committee stay abreast of pending financial reporting and regulatory developments and understand how they may affect the company? For example, does it consider the nature of SEC comment letters being issued to companies in the industry?
- Does the committee give adequate attention to overseeing the following areas:
  - The financial reporting process, including reviewing annual and quarterly financial statements, earnings releases (including management’s discussion and analysis (MD&A), information and guidance provided to analysts and rating agencies, and pro forma or “adjusted” non-GAAP information in releases)?
  - Critical accounting policies, quality of management judgments and estimates impacting the financial statements, and written communications between external and internal auditors and management?
  - Implementation of new accounting standards?
  - Adequacy of disclosures of significant transactions involving related parties?
  - Existence of significant pressure to meet budgeted or expected targets?
  - Consideration of fraud risk, including the risk of fraudulent financial reporting?
  - Management’s purpose for reporting non-GAAP and other key operational measures in public reports and the disclosure controls and procedures for ensuring their propriety, accuracy and consistency with prior periods?
- Is the committee satisfied that the following statements are true:
  - Appropriate financial reporting controls and disclosure controls and procedures are in place?
  - It is being notified of any significant deficiencies and material weaknesses on a timely basis and is kept informed of steps taken along the timetable for correction?
  - It is notified promptly of significant compliance issues and briefed regularly on the status of outstanding issues and their remediation?

## Oversight of the External Auditor

Does the committee give adequate attention to the following areas in conjunction with ensuring audit quality:

- Hiring, retention, performance and compensation of the external auditor, including preapproval of nonaudit services to be provided by the auditor?
- Approving policies on hiring personnel from the external auditor (with an appropriate cooling-off period)?

- Setting the tone for the company's relationship with the external auditor in preserving auditor objectivity, in part, through direct oversight of the audit relationship and evaluating the auditor's independence?
- Evaluating the propriety of nonaudit services (including those provided in the environmental, social and governance (ESG) space when the auditor is attesting to ESG disclosures) in view of the SEC's expectation of increased PCAOB focus on auditor independence?
- Meeting periodically with the lead audit partner(s) and the specialists (e.g., tax, IT, valuation, actuarial) who contribute to the audit process and, when necessary, engaging in dialogue outside of formal committee meetings?
- Defining expectations regarding the nature, method and frequency of communication from the auditor, particularly with respect to critical audit matters (CAMs)?
- Understanding the process to report CAMs and whether they represent significant judgmental matters due to their nature or represent issues on which management and the auditor may not agree or if management may be applying aggressive accounting — indicating an opportunity to streamline and improve the quality of the company's accounting and reporting processes?

## Risk Oversight

- Does the audit committee understand the company's risk profile and discuss with management the company's policies related to risk assessment and risk management?
- If the audit committee takes on only those risk oversight responsibilities that address the risks inherent in the committee's chartered activities (e.g., financial reporting, fraud, reputation, and certain compliance, technology and other risks), does it collaborate with other board committees and the full board to ensure that significant risks are not overlooked by the board in its overall risk oversight, such as:
  - Cybersecurity risk?
  - Compliance risk?
  - Data privacy risk?
  - Third-party risk?
- If the board delegates its overall risk oversight responsibilities to the audit committee, is the committee able to devote sufficient time to the risk oversight process as well as to its other responsibilities? Does the committee:
  - Allow sufficient time to monitor the strength of the company's risk governance and culture?
  - Periodically review management's assessment of the top enterprise risks, including the member of management who owns each risk and the board committee responsible for overseeing each risk?
  - Ensure that management has in place a reasonable information and reporting system with regard to the critical enterprise risks that warrant attention and that the committee is privy to its insights from time to time and whenever necessary?
  - Periodically assess the quality and reliability of the risk information it receives?

- Periodically discuss with management whether the appropriate “tone at the top” is reinforcing the company’s values and promoting a “risk-aware” culture?
- Work with the compensation committee to understand the implications of existing incentive compensation plans to the undertaking of risk?
- If the audit committee oversees cybersecurity, does it have access to sufficient cybersecurity expertise?
- Regardless of the scope of risk oversight, as designated by the full board, are committee members satisfied that they:
  - Understand the business, technology and other risks that could affect financial and public reporting?
  - Receive appropriate overviews from business leaders concerning matters germane to financial risks and other factors influencing the financial statements?

## Business Context

Does the audit committee have a strong business context to discharge its responsibilities effectively? For example, does it consider:

- Changes in the business environment that can result in reconsidering financial reporting assertions and create different financial reporting risks?
- Significant and rapid expansion of operations or unusual disruptions that can strain the control environment and increase the risk of a breakdown in key controls?
- Changes in the control environment, including tone at the top and alignment with the tone in the middle, that could affect its overall effectiveness?
- New business models, products or activities that may introduce new risks associated with financial reporting?
- New disclosure requirements, accounting pronouncements and tax regulations?
- Other relevant aspects of the business environment that present change from the prior year that could have financial reporting implications, such as increased credit risk, inventory write-downs, asset impairments, and recording and disclosure of loss contingencies?

## Corporate Culture

Unless responsibility is delegated to one or more other board committees, does the audit committee oversee:

- The organization’s ethics and legal compliance policies, including its code of conduct and tone at the top set by management regarding ethical and responsible business behavior?
- The adequacy of the organization’s confidential, anonymous hotlines and other procedures for handling complaints and employee concerns on accounting, financial reporting, internal controls,

auditing and code of conduct matters, and compliance with applicable laws, regulations and internal policies?

- The initiation of internal and independent investigations on matters within the committee’s scope of responsibilities?
- The handling of management’s override of established controls and waivers of conflict-of-interest policies, including the risk mitigation and control mechanisms in place?

## **Executive Sessions**

- Are audit committee meetings preceded or followed by private sessions with the CFO, the chief audit executive (CAE) and the independent auditor?
- Does the committee meet in a closed executive session for its members to discuss:
  - Issues of concern, how the meeting went and agenda topics to cover in future meetings?
  - Evaluation of the CFO and other finance executives?
  - Evaluation of the CAE?

## **Environmental, Social and Governance (ESG) Reporting**

- Has the committee collaborated with the board and various committee chairs to ensure that the board has sufficient overall input into ESG/sustainability performance, reporting and disclosures?
- Has the committee considered the implications of the company’s human capital, climate and other ESG disclosures on the assumptions underlying financial reporting assertions?
- Does the committee engage with management on disclosure controls and procedures (sometimes referred to as “internal control over sustainability reporting”) relating to ESG metrics and reporting?
- If the company opts to obtain assurance, does the committee ensure that there is appropriate board oversight over such activities, including ensuring external auditor independence?

## **Oversight of Finance Organization**

Does the committee:

- Discuss succession planning for the CFO and finance staff, including the finance function’s bench strength?
- Understand finance’s process for early identification and resolution of accounting and other issues?
- Understand plans to address new accounting and reporting requirements and related risks?
- Provide input into the finance organization’s goal-setting process?

## Oversight of Internal Audit

Does the committee:

- Ensure that the CAE has direct reporting access to it?
- Play an active role in determining the highest and best use of internal audit, as well as the appropriate structure of the group (e.g., in-house versus outsourced resources)?
- Have transparency into the internal audit risk assessment and audit plans, including activities and objectives regarding internal control over financial reporting?
- Understand internal audit staffing, funding and succession planning, particularly the adequacy of resources to deliver on the audit plan?

## Committee Effectiveness

- Prior to reporting on its activities to the full board and/or to shareholders, is the committee satisfied a process is in place to ensure that all matters in the committee charter are covered sufficiently by its activities?
- Do committee members have the time to do their jobs effectively and fulfill the responsibilities specified by the charter?
- Does the committee serve as an advocate for financial reporting in working with other board committees and the full board to monitor execution of corporate initiatives, such as cost-reduction plans as well as enterprise resource planning (ERP)/financial system implementations, so that they are not unintentionally implemented in ways that would compromise management meeting its financial reporting responsibilities?
- Regarding committee meetings:
  - Are briefings and other materials distributed well in advance? Do committee members review those materials prior to meetings?
  - Do reports include executive summaries that highlight issues and critical discussion points to allow for discussion (versus presentation) during meetings?
  - Do meetings allow open and candid discussions among attendees?
- If a member serves simultaneously on multiple audit committees (say, for more than three public companies), has the board considered whether that individual is able to devote sufficient time and attention to the items on the company's audit committee agenda?
- At least annually, does the committee:
  - Perform a robust self-assessment, including the contribution and performance of individual members, and are the results discussed with committee members in executive session and plans developed to implement improvements?
  - Review its overall responsibilities to ensure that its workload is manageable?
  - Obtain informal feedback from the board, the CEO, the CFO and external auditors as to how it can best contribute value?

## Member Orientation and Education

Does the committee:

- Ensure that new members receive orientation that directs attention on the chartered responsibilities, agenda and focus; the company's business; and its most significant accounting and reporting issues?
- Include educational topics on the agenda periodically (e.g., a deep dive on a specific area of the business and related risks, or a refresher in a significant accounting area)?
- Address board education requirements in accordance with the company's corporate governance guidelines and consistent with applicable listing standards?

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