

On being a successful audit committee chair

By Frederick D. Lipman

Spencer Stuart / DirectorS & Boar DS Director S r oSter 20 directors & boards T he Sarbanes-Oxley Act of 2002 (SOX) transferred pow- ers from the management of a public company to its inde- pendent audit committee. The chair of the audit committee has the important role of providing leadership for the audit committee and of exercising powers on behalf of the committee previously re- served to management. Today, success- ful audit committee chairs are taking a broader view of their respon- sibilities beyond the technical legal requirements of SOX or SEC or exchange listing rules and are attempting to follow what are developing as best practices. Some of the best practices being implemented today include the following:

1. Audit Committee Com- position. The successful chair should be concerned about the quality and competencies of the audit committee mem- bers. We all know about the requirement for a financial expert imposed by exchange listing rules and SEC disclo- sure requirements. However, it is not necessary, or even de- sirable, to require that every member of the committee be an account- ing expert. Persons with knowledge of the industry and familiarity with company operations can be valuable members even if they are not financial experts, as- suming that they have basic accounting knowledge. Moreover, successful audit committee chair are evaluating the con- tributions of their committee members at least annually and recommending neces- sary changes where appropriate.
2. Internal Audit. It is a best practice for the head of the internal audit function to be hired by the audit committee, report directly to the audit committee, and be subject to dismissal by the audit commit- tee. This best practice has, on occasion, created conflicts with management who, under this arrangement, may view the in- ternal auditor as not part of the manage- ment team. A successful audit commit- tee chair must anticipate these potential conflicts, devise methods to insure that there is a good rap- port between and among the internal auditor, the CFO, and the chief accounting officer, and make certain that all par- ties understand their respec- tive roles. The audit commit- tee chair should also inquire periodically from the internal auditor as to the adequacy of staffing of the internal audit function. The chair and the internal auditor should ex- change cell phone numbers and email addresses.
3. Coordination with In- d e p e n d e n t A u d i t o r. T h e c h a i r s h o u l d h a v e a g o o d w o r k i n g r e l a t i o n s h i p w i t h t h e p a r t n e r a n d m a n a g e r o f t h e i n d e p e n d e n t a u d i t o r s o t h a t a n y p r o b l e m s c a n b e a n t i c i p a t e d a n d a n y f r i c t i o n w i t h m a n a g e m e n t o r t h e i n t e r n a l a u d i t o r q u i c k l y r e s o l v e d. T h e c h a i r s h o u l d s c h e d u l e p r i v a t e m e e t i n g s w i t h t h e i n d e p e n d e n t a u d i t o r s a n d a n n u a l l y h a v e a r o b u s t d i s c u s s i o n o f a n y i n d e p e n -

dence issues. 4. Educating the CFO. Many CFOs are uncertain as to what the audit committee expects from them. The successful chair, after consulting with the full committee, must have an open and candid dialogue with the CFO, preferably privately on a one-on-one basis, which would include at least the following topics: (a) the specific types of information the audit committee requires to perform its function, with the understanding that this information needs constant refinement (and too much information is as bad as too little information); (b) what public documents, such as press releases and periodic SEC filings, does the audit committee wish to review prior to publication or SEC filing, and the time frames in which such information is to be supplied to the audit committee; (c) the expectations of the committee for the CFO to immediately communicate material financial developments within the company; and (d) what monitoring of the services of the independent auditor and the costs of such services should be provided by the CFO.

5. Audit Committee Procedure. The successful chair will attempt to develop a consensus among the audit committee members on all important issues and will suggest the need, when appropriate, for special consultants, including independent counsel. The chair will obtain recommendations from the audit committee members as to the number and length of meetings and, with the assistance of the internal auditor, develop an agenda for each meeting. The chair should schedule an annual meeting with the head of both the sales and tax departments and an annual self-evaluation of the audit committee, including a review of the audit committee charter. Finally, the successful chair should insist upon the continuing education of all new and old audit committee members on internal accounting issues and on new accounting pronouncements. ■ The author can be contacted at lipman@blankrome.com. His latest book, *Executive Compensation Best Practices*, co-authored with Steven Hall, was published in April 2008 by John Wiley & Sons Inc. at Your Be St Frederick D. Lipman is president, Association of Audit Committee Members Inc. (www.aacmi.org) and partner, Blank Rome LLP, an international law firm (www.blankrome.com). On being a successful audit committee chair Five best practices being implemented today. BY Frederick D. Lipman