

Audit Committee *Brief*



Charting the Course: Audit Committee Annual Activities

As the SEC filing season draws to a close, audit committees should set aside time to perform some important activities to prepare for the coming fiscal year. These typically center around three interconnected areas: undergoing a performance evaluation, reviewing the charter, and setting the calendar and associated meeting agendas for the next 12 months.

Coordinating these activities allows audit committees to reflect on the past year's performance while refining the roles, responsibilities, and timeline for the coming year. This issue of the *Audit Committee Brief* highlights requirements, leading practices, and resources for audit committee members as they undertake this process.

Leading practices for audit committee financial literacy

- Understand auditing, accounting, and financial reporting issues relevant to the company and how members of management and the independent auditor address them.
- Consider and plan for financial reporting and regulatory developments that may affect the company, and particularly its talent needs.
- Focus on committee composition issues, including risk management, independence, business and leadership experience, and succession planning.



Audit committee annual performance evaluation

NYSE listing standards require audit committees to undergo an annual performance evaluation, and for this responsibility to be reflected in the committee's charter. When led internally, the process can be managed by any of a number of parties, including the audit committee itself, the overall board, or the nominating/governance committee. Some audit committees engage an external party to assist with the evaluation. A combination of approaches may prove optimal in obtaining a fresh perspective. For example, the audit committee may opt to engage an external adviser every two or three years and to conduct the process internally in the intervening years.

The format of the evaluation will vary based on the approach chosen. For self-assessments, committee members can complete a questionnaire collectively or individually. If a different group is involved in the assessment, the format may include evaluation forms, interviews, or both. The party leading the evaluation often solicits information from individuals who have interacted significantly with the audit committee, such as the CEO, CFO, general counsel, and independent auditors. A combination of self-assessment and assessment by other groups is frequently most effective and can yield robust perspectives.

The evaluation process should also include a determination of whether the committee is receiving the right information to make informed decisions. It can be helpful to evaluate whether board books can be enhanced through the inclusion of different data.

The results of the evaluation can be used to reengineer processes, procedures, and agendas, and can strongly influence where the committee spends its time. A well-designed assessment can provide numerous benefits, including:

- Tailoring agendas and meetings to focus on the most critical issues
- Shifting compliance oversight to occur between regular, in-person meetings
- Regularly evaluating the committee's composition in the context of emerging financial reporting issues
- Optimizing the timing, level of detail, and quality of materials provided by management
- Identifying topics and mechanisms for continuing education.

Deloitte has developed a [questionnaire](#) to assist with audit committee self-assessments. The [Performance Evaluations](#) section of the Deloitte Center for Corporate Governance website features several additional tools and resources.

Audit committee charter

The audit committee charter formalizes the framework for the committee's oversight and risk management responsibilities. In addition to addressing the activities required by regulations, the charter should highlight the committee's recurring activities and its responsibility for significant transactions and unusual events.

Though many aspects of the charter will remain unchanged from year to year, there are several circumstances in which updates may be needed, including:

- Changes in regulatory or legal requirements
- The assignment of new or legal responsibilities to the audit committee or realignment of responsibilities not required to be performed by the committee
- The addition of new practices the committee wishes to include among its responsibilities
- Changes in company bylaws affecting the composition or appointment methodology of the committee.

NYSE charter requirements. The NYSE requires the charter to provide for oversight of the company's financial statements, compliance with legal and regulatory requirements, the independent auditor's qualifications and independence, and the performance of internal audit and the independent auditor.

Charters of NYSE-listed companies must also describe the committee's responsibility to:

- Prepare the audit committee report for the proxy
- Discuss policies regarding risk assessment and management
- Discuss earnings releases and information provided to analysts and rating agencies
- Participate in private sessions with management, internal audit, and the independent auditor
- Annually assess the audit committee's performance (see preceding section on evaluation for further details)
- Comply with Rule 10A-3(b) of the Exchange Act and other responsibilities required by NYSE listing standards.

NASDAQ charter requirements. An annual review of the charter is required for NASDAQ-listed entities. The NASDAQ requires that the charter lay out the committee's oversight of the company's accounting and financial reporting processes and the audits of its financial statements. The charter should also address the committee's scope of responsibilities and how it carries them out, including structure, processes, and membership requirements. The responsibilities delineated in the charter must include:

- Overseeing auditor independence and requesting a written statement from the independent auditor disclosing all relationships with the company, in accordance with PCAOB Ethics and Independence Rule 3526
- Communicating with the independent auditor about relationships or services that could affect the auditor's objectivity and independence
- Carrying out the requirements of Rule 10A-3(b) of the Exchange Act.

SEC disclosure requirements. SEC rules require public companies to disclose in their proxy statements whether the board has adopted a written charter for the audit committee and whether a copy of the charter is available on the company's website.

Based on a review of Fortune 1000 company charters and an analysis of regulatory requirements, Deloitte has developed a [sample charter](#) to assist in preparing, reviewing, and updating the charter.

Audit committee calendar and meeting agendas

Concurrent with, and informed by, the charter review and annual evaluation process, the committee can examine its annual calendar and consider modifications based on emerging issues. The committee may also wish to evaluate the appropriateness, frequency, and timing of activities already on the calendar. The charter should allow for the audit committee to meet outside the official calendar as needed.

Agenda items will vary significantly by company and industry. In addition to recurring topics such as the review of quarterly and annual SEC filings and preapproval of fees to be paid to the independent public accounting firm, examples of areas to consider include:

- Tone at the top, including a code-of-conduct review
- Tax accounting
- Enterprise risk management and risk oversight
- IT assessment and strategy
- Business continuity and disaster recovery
- Incentive compensation
- Employee benefit plan review
- Joint venture and affiliate review
- Accounting hot topics
- Reviews of significant accounting estimates and management judgments
- IFRS/U.S. GAAP convergence status
- Sustainability
- Internal audit plan and assessment
- Dodd-Frank provisions
- Investment portfolio review
- Qualitative risk disclosures
- Insurance coverage review
- Succession planning
- Finance personnel evaluation
- Litigation review with chief legal counsel
- Third-party compliance programs
- Hedging policies
- Emerging global risks
- Related-party transaction review
- Review of shared services center

Audit committees can benefit from aligning meeting materials and agendas with priority areas.

Significant matters requiring review and comment can be positioned at the beginning of advance materials and agendas. In turn, non-urgent compliance matters, standard reports, and informational items can often be presented at the end of materials and meetings, as they may not always need to be discussed.

In making updates to the calendar and charter, the audit committee should consider consulting with management, the internal auditors, the independent auditor, and, when appropriate, legal counsel.

Refer to Deloitte's [Top Issues for Audit Committees in 2013](#) for additional information and resources related to emerging agenda topics. A [planning tool](#) for designing a calendar of audit committee activities is also available through Deloitte's Center for Corporate Governance website.



In other news

FASB and IASB preparing to issue final standard on revenue recognition

The FASB and IASB are completing deliberations on their November 2011 revised exposure draft *Revenue from Contracts with Customers* and plan to jointly issue a final standard in the second quarter of 2013. The standard will outline a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and will supersede most current revenue recognition guidance.

Please see Deloitte's [March 5](#) issue of *Heads Up* for further details on the proposed revenue recognition model.



Conclusion

A carefully planned process for audit committee performance evaluations, charter reviews, and agenda refinements can yield substantial benefits, including enhanced knowledge and information gathering, improved procedures, and more productive audit committee meetings. These results are maximized when committees go beyond focusing only on compliance efforts and frame their year-round activities as opportunities for improvement. Periodically evaluating the approach to conducting these activities helps confirm that the right issues receive the proper amount of attention each year.

Additional resources



[Audit Committee Performance Evaluation](#)



[Financial Literacy Self-Assessment Tool](#)



[Sample Audit Committee Charter](#)



[Planning Tool: Audit Committee Calendar of Activities](#)



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[Top Issues for Audit Committees in 2013](#)



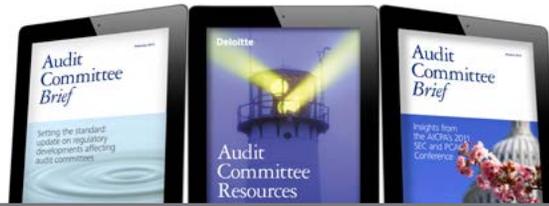
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