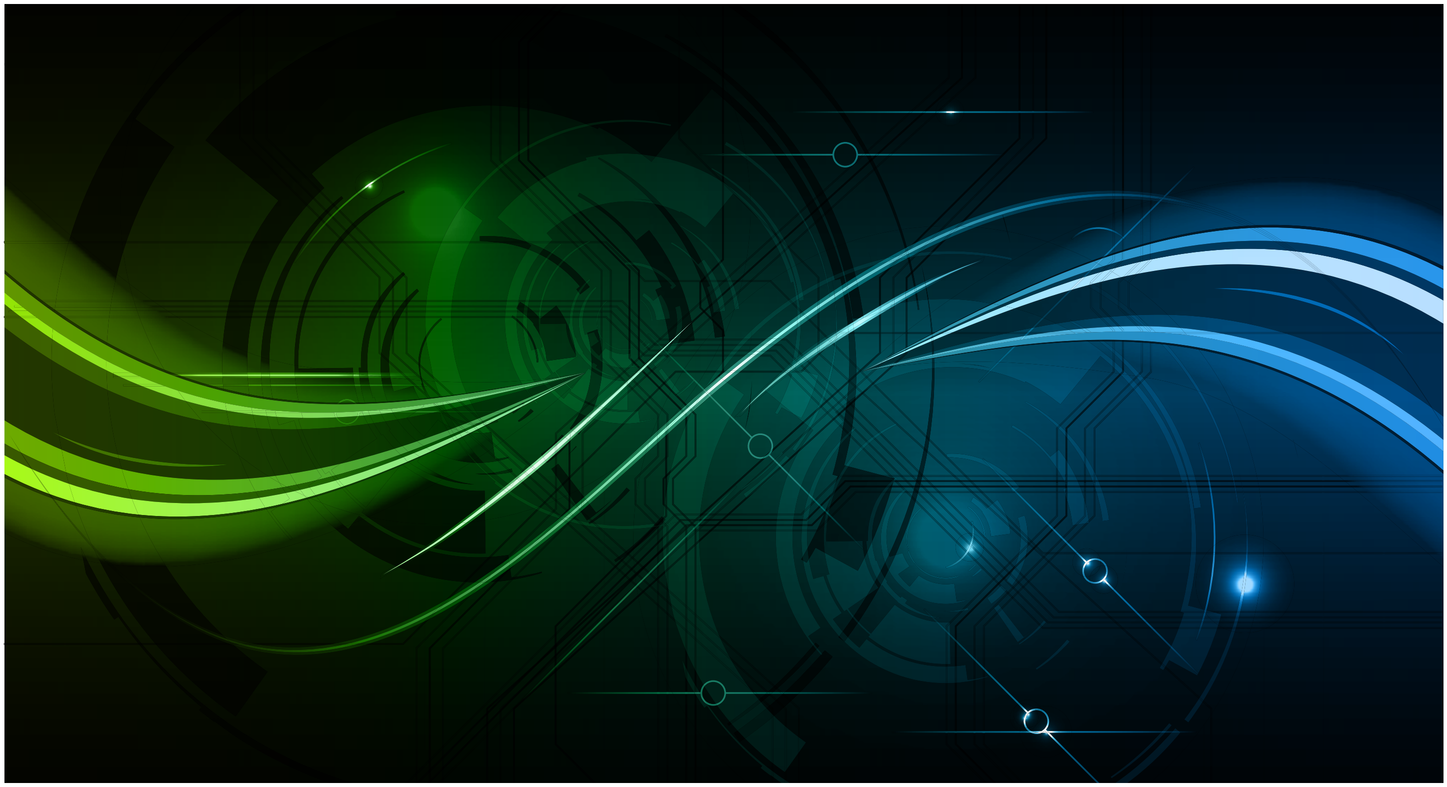

What audit committees really want from CFOs

For some CFOs, preparing to appear before the audit committee may conjure memories of final exams or first job interviews. Indeed, CFOs' quarterly presentations before the audit committee could be seen as a test of sorts.

The audit committee's responsibilities are broad, ranging from reviewing management's approach to enterprise risk, to understanding financial reporting disclosures, to evaluating its processes and controls and compliance matters, to assessing the performance of its external and internal auditors, and beyond. Furthermore, many aspects of the committee's work is shaped by rules and regulations issued by a combination of the U.S. Securities and Exchange Commission (SEC), the listing exchanges, and other regulators specific to the company. For CFOs, whose role includes guiding the committee through the company's financial results and reporting on its risk management activities, it can be difficult to figure out where to begin and how to end.

Additionally, the sense of urgency that drove the priorities of both CFOs and audit committees in recent years, as they strategized their way through a once-in-a-lifetime global pandemic and the switch to remote work practically overnight, added to the complexity and regularity of CFO and committee interactions. With those lifetime events showing signs of subsiding, the frequency of meetings has stopped increasing. The average number of audit committee meetings among S&P 500 companies rose to 8.4 a year in 2021, but has since retreated to 8.2, according to a recent study.[1]

But in the midst of regulatory developments, rising interest rates, and simmering geopolitical tensions, CFOs still face a formidable challenge in keeping audit committees updated as they explain the financial implications of evolving threats and intensifying market forces and, of course, the company's performance or lack thereof. Not only do CFOs have the task of deciding which details are most critical to communicate, but they also face the expectations to deliver it all succinctly and confidently in a limited amount of time.

After a meeting, CFOs might wonder: Did I use the audit committee's time productively, fulfilling its expectations? Would the committee members say I provided them with an effective level of information to vote on certain actions, or saddled them with more piles of data?

In this edition of *CFO Insights,* we'll synthesize what we've learned from engaging CFOs in our labs and forums and from interviewing audit committee chairs and members as part of our CFO Program's CFO Transition Lab™ offering, as well as through other client interactions, to provide CFOs with general answers to that seminal question: What do audit committees *really* want?

1. No surprises

Recent crises have not softened the attitude of audit chairs and committee members toward the unexpected. They do not want surprises.

Unpredictable things will happen, of course. And when they do, CFOs need to have a strong relationship and trust with the audit committee and clearly communicate in a timely and candid manner so the committee isn't caught off guard. To set the context for direct, timely communications and joint problem-solving, CFOs should consider building strong working relationships early in their dealings with the audit committee. They may want to establish regular communications with the audit chair. Such interactions can happen formally or informally and may require additional time outside of audit committee meetings.

Audit chairs typically see acting as a sounding board and being accessible to the CFO at any time as integral to their roles as effective chairs. By establishing a good relationship with audit chairs early on, CFOs can enhance mutual confidence in tackling difficult issues when they arise.

2. Strong partnering with the CEO and other leaders

Audit committees and the overall board want to see a CFO who effectively partners with the CEO and other key business leaders. Understandably, CFOs say their relationship with the CEO is the most important to their own success, according to Deloitte's North American 4Q21 *CFO Signals™* survey.[2]

To borrow from Deloitte's Four faces of the CFO framework, some CEOs and boards prefer their CFO to focus on the traditional roles of operator and steward, while others look for support from the finance chief as a strategist and catalyst. In the 4Q21 *CFO Signals* survey, 21% of surveyed CFOs say they would most like to improve their relationship with the CEO.[3]

As a strategist, a CFO can align financial strategy to business strategy for growth but may also choose to shape growth through finance (for example, finding innovative ways to finance M&A or other investment activity or pricing strategies to grow revenues). Similarly, CFOs can drive change in organizations through pulling certain levers, such as efficiency initiatives and new ways of measuring and rewarding performance. Effective partnering and influence skills with the CEO and other C-suite leaders are critical imperatives for CFOs. In fact, audit chairs and board members often observe CFO-CEO and CFO-peer relationships to gauge how well the leadership team works together to achieve company goals. In companies undergoing transformation, CFOs may be tapped to serve in a key leadership role. In the 2Q21 *CFO Signals* survey, 42% of surveyed CFOs said their primary role in a transformation was to serve as a co-leader, while 16% identified themselves as the leader.[4]

3. Confidence in finance organization talent

As the workhorse for creating accurate and timely financial reports, the broader finance organization is of interest to audit committees. They want to know that the finance organization is stable and supports and complements the skills of the CFO. They also want assurances that key-person risks are being managed and that the organization is developing finance talent, including potential successors to the finance chief.

Occasionally, audit committee members may visit with key finance leaders in advance of a scheduled meeting to gauge the state of the finance organization. At other times, they may want the opportunity to hear from and observe select finance staff at audit committee meetings on a particular topic, such as forecasting.

A good practice for CFOs is to give the audit committee visibility into their key staff and have candid discussions on how they intend to develop talent. It's also important to convey plans to change staff well ahead of time to forestall misunderstandings with committee members. CFOs and audit committees also should discuss succession planning at least once a year, typically in an executive session. It's important to keep communications with the committee in balance (see accompanying story, "Less than leading practices: What audit committees *don't* want from CFOs").

4. Command of key accounting, finance, and business issues

CFOs need to have full command of the key technical accounting, financial reporting, tax compliance and planning, control environment, finance, or treasury issues pertinent to their companies—within the C-suite, with the board and audit committee, and with broader stakeholders.

CFOs who are new to the role, if not the company, need more than an accounting background. They may also need to make sure they are up to speed on the business, focusing on understanding the critical business issues and company business model. CFOs joining a diversified company where they may lack familiarity with the business model of select units in the portfolio, will likely benefit from deep dives that can help them gain the requisite command over pertinent issues.

CFOs who come to the role with finance or operating business backgrounds may also need to take additional steps. For an incoming CFO with a non-accounting background, a good practice is to schedule a series of deep dives with expert staff or outside resources, such as the company's auditors, to come up to speed on critical financial reporting, control, or technical accounting issues, as well as tax issues. This practice establishes both a structure and timeline toward mastering key issues. Moreover, by sharing the timelines and lessons learned from those sessions, the CFO can continue to gain the audit committee's confidence and manage expectations.

The audit committee may also focus on bringing the right complement of people to supplement the CFO's experience and skills. For example, an incoming CFO who doesn't have the requisite experience in accounting and financial reporting can be partnered with a chief accounting officer who can manage those areas, co-owning them with the audit committee.

5. Insightful forecasting and earnings guidance

Audit committees frequently express the need for CFOs to take ownership of improving forecasting and budgeting to deliver more effective guidance on future cash flows and avoid earnings misses (see "Getting ahead: How CFOs can align minds and machines to reinvent forecasting," *CFO Insights,* Oct. 20, 2022).

But beyond forecasts and guidance, what many audit committees really want is an insightful CFO—one who can clearly articulate the underlying assumptions and drivers that guide estimates of future performance. They seek a CFO who can not only articulate the drivers of future performance, but also provide them with a convincing story on how the business will execute on the drivers to deliver performance or mitigate risks. To effectively perform this function, CFOs likely need to join other C-suite members in discussions of the company's strategy, performance, and outlook. The committee wants to ensure that the CFO has the right marketplace mindset to get ahead of what is coming in the economy or global marketplace.

6. Effective risk management

Some audit committees expect the CFO to take a leading role in managing enterprise and operational risk beyond traditional financial, accounting, and regulatory compliance risks.

The CFO will likely be charged with setting the tone in terms of ethics and integrity, overseeing the control environment, and ensuring the right people are deployed across the organization to support compliance. The CFO is often most on point to coordinate this message on organizational risk management to the board constituents—including the audit committee and others. In companies where there is no chief risk officer, CFOs often lead the risk management process, serving as the primary liaise to the audit committee (to find out where audit committees are most active, see Figure 1). The committee wants to make sure that the finance chief is monitoring risks and sensing new ones, bringing them to the audit committee's attention. From there, there's often a dialogue about where those specific risks should be overseen across the governance structure. Working with the audit committee, the CFO should make sure that most material risks are being discussed at the board level.

Figure 1. Lines of duty: Which board committees do what

Indicate where primary oversight of the following areas resides among the board and its committees, and whether any modifications have been made to the delegation of primary oversight in the past year. [Select all that apply.] *Survey consists of nearly 180 public companies.*

Shading indicates results ≥30%.	Full board	Audit committee (or similar)	Compensation committee (or similar)	Nominating and Governance committee (or similar)	Risk committee (or similar)	Other committee	N/A	Oversight changed; it is now primarily at the full board-level	Oversight changed; it is now primarily at the committee-level	No change to oversight, but we are considering or have considered doing so
Enterprise risk management (ERM)	44%	50%	1%	4%	18%	1%	1%	0%	1%	5%
Climate change, water, and other environmental	25%	5%	1%	58%	9%	14%	1%	1%	5%	6%
Political spending	13%	2%	0%	47%	0%	7%	28%	1%	4%	2%
Community impacts/relations	21%	1%	3%	45%	2%	9%	16%	1%	1%	4%
Human capital/workforce/talent	19%	2%	75%	9%	0%	1%	2%	0%	5%	4%
Workforce DEI (diversity, equity, and inclusion)	24%	1%	66%	24%	0%	1%	1%	0%	6%	4%
Corporate culture	47%	1%	29%	14%	0%	3%	10%	1%	2%	4%
Shareholder proposals	24%	1%	4%	71%	1%	1%	6%	0%	1%	4%
Shareholder engagement	28%	1%	11%	61%	0%	4%	5%	0%	0%	4%
Cybersecurity	30%	61%	1%	2%	16%	6%	0%	1%	3%	4%
Technology strategy (e.g., IT infrastructure, innovative and disruptive technology, social media)	44%	29%	0%	2%	10%	13%	9%	1%	1%	3%
Corporate compliance and ethics	15%	57%	5%	32%	6%	1%	0%	1%	1%	3%
Legal and regulatory	45%	44%	4%	22%	9%	5%	4%	0%	0%	1%

Source: Back to basics: Board committees, *Board Practices Quarterly*, Society for Corporate Governance and Deloitte Development LLC, June 2022.

In addition, the audit committee will want to know that reporting lines are clear across the organization and that the organization structure encourages the right behaviors and timely flow of risk information. This need is especially critical in the case of large multinational organizations, where finance resources may be in a direct reporting line to local business leaders versus the global CFO. In these cases, the audit committee may want to make sure the right incentives and structures are in place to mitigate risks.

The CFO and finance organization may also work to hedge against or mitigate operational risks, such as those related to cybersecurity, inflation, or supply chain disruptions. Risk is dynamic, and the CFO is a key resource for the board to understand the organization's risk posture and risk mitigation strategy.

CFOs who lead risk management may also head up a risk management committee, bringing together leaders who own the material risks. Even CFOs who are not in charge of risk may find it useful to participate in such a meeting.

7. Clear and concise stakeholder communications

This edition of *CFO Insights* began with the importance of establishing timely communications with the audit committee to effectively forestall surprises and other unexpected issues from escalating. Beyond a regular sequence of communications, audit committee members tell us they want CFOs to be effective communicators—with the committee and board, the investor community, and other external and critical stakeholders.

Audit committees generally expect clear and concise communications from CFOs that put the numbers and risks in context, offering fresh insights. In addition, communications with analysts and investors should demonstrate their mastery over the pertinent business, financial, and accounting issues. Specifically, CFOs have to provide insight into key drivers of future performance and convey how they will work to deliver results to the market.

Less than leading practices: What audit committees *don't* want from CFOs

How bad meetings happen to good CFOs

- **Get exposure for your finance team—but not all at once**. Audit committee meetings often include varied constituents sitting around a table: external audit, internal audit, the management team, the legal function, and others. While there may be times when it's appropriate for the CFO to invite the controller or the VP of financial reporting, CFOs should avoid bringing too many team members at once. It's important for the audit chair to know who is in attendance, even the folks standing up in back. A crowd is likely to inhibit any candid back-and-forth. If several members of the finance team have a role in a single meeting, each should exit after they've done their part.
- **Strategic thinking comes packaged in brevity and synthesis**. CFOs may be tempted to share their commanding knowledge of the business or the industry or both. And more. But with minutes at a premium, CFOs can be more useful by, say, boiling their presentation down to three strategic objectives, then tying them back to the company's financial statements.
- **Look for input, rather than seeking validation**. Committee members typically want to participate in healthy debate, bringing their own experience and expertise to the table. CFOs should come to the audit committee with a proposed solution, then engage the committee members in helping finalize a decision. When a CFO comes prepared with different proposals around implementing a dividend strategy, for example, committee members can share valuable observations regarding how the market and analysts might react.
- **Don't recreate three-ring binders**. Nobody's interested in lugging around the pre-reading in an overstuffed loose-leaf notebook—even a virtual one. While CFOs and others may assign the committee more pre-reading than in the past, they should do so using software or notebook computers which are loaded with the main material and deck. It's important to make sure that pre-reads contain the right level of information—strategic, with an executive summary of what is included in each section, and clear indications of areas of focus or actions.
- **Accept coaching, whether or not you agree you need it**. The audit committee chair is responsible for keeping the mechanics of the meeting well-oiled. If a CFO's presentation comes across as unfocused or tedious, for instance, a supportive committee chair will take steps to offer constructive feedback and coaching. Effective CFO communications can help the full audit committee be more effective.

Having strong investor relations and communications support is a must in addressing these needs. Often, it seems, CFOs may find they need to sharpen their communications strategy across key stakeholders, perhaps intially underestimating the level of effort required to undertake effective communications with them. Developing a communications strategy early can help build confidence with the board as well as other critical stakeholders, including Wall Street investors and analysts.

Audit committees play a critical corporate governance and oversight role. Their members can also bring a wealth of experience to CFOs. Attending early to the above requirements can create a context for both parties to effectively work together—making their meetings not only worthwhile but also productive.

End notes

1. 2022 U.S. Spencer Stuart Board Index, Oct. 2022.
2. CFO Signals™: 4Q 2021, CFO Program, Deloitte LLP.
3. Ibid.
4. CFO Signals™: 2Q 2021, CFO Program, Deloitte LLP.

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